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IN THE SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1993

PAUL W. BONAPFEL, Chapter 7 Trustee
for the Bankruptcy Estate of
CARPET CENTER LEASING CO., INC.,
PETITIONER

v.

NALLEY MOTOR TRUCKS, a Division of
NALLEY CHEVROLET, INC.,
RESPONDENT

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Whether § 507(b) of the Bankruptcy Code preempts state law so as to create an administrative expense claim in favor of a prepetition secured creditor whose claim against a debtor is barred under applicable state law?

2. Whether the award of an administrative expense priority under § 507(b) to a prepetition secured creditor is in direct conflict with the plain meaning of § 361(3)?

PARTIES TO THE PROCEEDING IN THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

Petitioner and Respondent were the sole parties in the proceedings before the United States Court of Appeals for the Eleventh Circuit. Pursuant to Sup.Ct.R. 29.1, Petitioner shows that he is an individual Chapter 7 Trustee for the bankruptcy estate of a corporation that has no parent companies or subsidiaries.

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NALLEY MOTOR TRUCKS, a Division of
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RESPONDENT

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

Paul W. Bonapfel, Chapter 7 Trustee for the bankruptcy estate of Carpet Center Leasing Co., Inc., respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this case.

OPINIONS BELOW

The United States Bankruptcy Court for the Northern District of Georgia, Rome Division, entered an order on March 12, 1991 awarding to Respondent an administrative expense priority claim pursuant to § 507(b) of the Bankruptcy Code in the amount of $370,915.96, the amount that Respondent claimed to have paid its predecessor in interest pursuant to a recourse obligation. This order

is included in Appendix C attached hereto, pages 32a through 34a. This decision was not reported.

Petitioner appealed to the United States District Court for the Northern District of Georgia, Rome Division. On January 31, 1992, the District Court entered an order affirming the award of the Bankruptcy Court in favor of Respondent. The District Court determined that the Bankruptcy Code and "federal equitable principles" create claims in favor of creditors without regard to state law. Therefore, it was irrelevant that Respondent was barred under state law from asserting a claim against the Debtor. The decision of the District Court is included in Appendix B attached hereto, pages 15a through 31a.

Petitioner appealed to the United States Court of Appeals for the Eleventh Circuit. The Court of Appeals affirmed the order of the District Court and held that Respondent, a prepetition secured creditor, was entitled to an administrative expense priority claim on account of the debtor-in-possession's use of trucks in which Respondent had a security interest during the period from the date of the filing of the bankruptcy case through the date that Petitioner was appointed trustee. The opinion of the Court of Appeals was entered on May 20, 1993 and is reported as *Paul W. Bonapfel, as Trustee for the estate of Carpet Center Leasing Company, Inc., v. Nalley Motor Trucks, a Division of Nalley Chevrolet, Paccar Financial Corp. (In re Carpet Center Leasing Company, Inc.)*, 991 F.2d 682 (11th Cir. 1993). This decision is included in Appendix A attached hereto, pages 1a through 14a.

Petitioner timely filed a "Petition for Rehearing and Suggestion of Rehearing *En Banc*." The petition was denied by the Court of Appeals for the Eleventh Circuit on September 30, 1993. The denial of the "Petition for Rehearing and Suggestion of Rehearing *En Banc*" is reported as *Paul W. Bonapfel, as Trustee for the estate of Carpet Leasing Company, Inc. v. Nalley Motor Trucks, a Division of Nalley Chevrolet, Paccar Financial Corp (In re Carpet Center Leasing Company, Inc.)*, 4 F.3d 940 (11th Cir. 1993). The denial of the "Petition for Rehearing and Suggestion of Rehearing *En Banc*" is included in Appendix D attached hereto, pages 35a through 37a.

STATEMENT OF GROUNDS ON WHICH JURISDICTION OF THIS COURT IS INVOKED

The judgment of the United States Court of Appeals for the Eleventh Circuit was entered on May 20, 1993. A "Petition for Rehearing and Suggestion of Rehearing *En Banc*" was denied on September 30, 1993. The time for petitioning this Court under Sup.Ct.R. 13 for a writ of certiorari runs from the date of the denial of the "Petition for Rehearing and Suggestion of Rehearing *En Banc*" and would expire at the close of business on December 29, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED IN THIS CASE

The following statutes are reprinted in pertinent part in Appendix E attached hereto, pages 38a through 43a: 11 U.S.C. § 361; 11 U.S.C. § 362; 11 U.S.C. § 502(b)(1); 11 U.S.C. § 503(b); 11 U.S.C. § 507(b); 11 U.S.C. § 558; Official Code of Georgia Annotated ("O.C.G.A.") § 10-1-36; O.C.G.A. § 11-9-504(3).

STATEMENT OF THE CASE

Carpet Center Leasing Company, Inc. ("Debtor") maintained a large fleet of trucks and trailers that were financed through numerous creditors, including Paccar Financial Corporation ("Paccar"), the predecessor in interest to Respondent. Debtor initiated a Chapter 11 bankruptcy by filing a petition on February 25, 1987. At that time, Debtor's fleet of trucks included twenty-six trucks in which Paccar asserted a security interest to secure ten separate installment contracts. The total monthly payment that Debtor was obligated to make to Paccar under the ten contracts was $39,267.37.

After the bankruptcy filing, Paccar filed a motion to lift the automatic stay, seeking authorization to exercise its state law rights with respect to its collateral. Paccar and Debtor subsequently

entered into a consent order that required Debtor to make monthly payments of adequate protection to Paccar in the amount of $18,661.25, approximately one-half the monthly amount due under the notes.[1] During the pendency of the case, Debtor paid Paccar approximately $108,500.00, resulting in three of the ten contracts being paid in full. Upon payment of the three contracts, the adequate protection payments were reduced to $15,890.80 per month.

Throughout the pendency of the Chapter 11 case, the Debtor failed to make payments of adequate protection to Paccar, as well as to the other creditors, in a timely manner. Despite the Debtor's failure to timely comply with the adequate protection arrangement, Paccar did not aggressively prosecute its remedies under the Bankruptcy Code. The Debtor's failure to make adequate protection payments to various creditors ultimately resulted in Petitioner being appointed Chapter 11 Trustee on March 4, 1988, over a year after the bankruptcy filing. At the time Petitioner was appointed, Paccar had a pending motion before the Bankruptcy Court seeking permission to exercise its state law rights with respect to the collateral. Petitioner immediately consented to an order that allowed Paccar to "foreclose its security interest in the aforesaid collateral in accordance with the laws of the State of Georgia or any other state in which the collateral is located."[2]

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[1] This consent order was entered on May 19, 1987.

[2] The Court of Appeals mistakenly states in its opinion of May 20, 1993 that "the [Petitioner] actively used Paccar's collateral throughout its postpetition possession...the [Petitioner] actually used the collateral to the benefit of the Debtor's estate." *Paul W. Bonapfel, as Trustee for the estate of Carpet Center Leasing Company, Inc. v. Nalley Motor Trucks, a division of Nalley of Chevrolet, Paccar Financial Corp. (In re Carpet Center Leasing Co., Inc.)*, 991 F.2d 682, 688 (11th Cir. 1993). This statement is plainly wrong. Both the Bankruptcy Court and the District Court recognized that *Petitioner* did not use any collateral following his appointment, as Petitioner never operated the business. Upon appointment, Petitioner immediately consented to relief from the state in favor of Paccar. Despite this obvious error, the Court of Appeals did not correct its mistake in its opinion denying Petitioner's "Petition for Rehearing and Suggestion of Rehearing *En Banc*."

Paccar exercised its rights under state law with respect to the trucks in which it held a security interest by repossessing the same during the end of March and the beginning of April of 1988. Paccar, however, failed to comply with the Georgia Motor Vehicle Sales Finance Act ("MVSFA"). Paccar also failed to comply with the Uniform Commercial Code as adopted in Georgia.[3] Following repossession of the collateral, Paccar held a public sale of the collateral on August 19, 1988. The only bidding for the collateral was by Paccar, which purchased the collateral for $89,000.00. There was no evidence that the public sale was advertised. Subsequent to the public sale, the trucks were sold to Arrow Truck Center, Inc. in an unadvertised private sale for a total of $60,000.00. Respondent paid to Paccar $370,915.96 pursuant to a recourse obligation.[4] Following payment under the recourse obligation, Paccar assigned its claims, if any, against the Debtor to Respondent.

Respondent asserted two claims against the Debtor. One claim was an alleged unsecured claim in the amount of $413,561.71. The other claim was a claim for a superpriority administrative expense in the exact same amount. The superpriority claim was ostensibly based on the diminution in value of the collateral in which Respondent asserted a security interest during the pendency of the Chapter 11 bankruptcy. Significantly, Respondent alleged in its motion for allowance of an administrative expense that its collateral decreased by an amount greater than the amount of its total claim, but acknowledged that any administrative expense claim to which it may have been entitled was limited to the total amount of its unsecured claim. Petitioner objected to the administrative expense

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[3] Paccar failed to timely send the required notices under the Motor Vehicle Sales Finance Act (O.C.G.A. § 10-1-36) and failed to establish compliance with the "commercially reasonable" sale requirements under the Georgia Commercial Code (O.C.G.A. § 11-9-504).

[4] Respondent sold trucks to Debtor, but the purchase price was funded by Paccar. The financing by Paccar was done with recourse, meaning that Paccar would be entitled to a claim against Respondent for losses suffered in connection with the financing of a particular sale.

claim and a hearing was held before the Bankruptcy Court on February 26, 1991. At the hearing, Petitioner argued that because Respondent, standing in the shoes of Paccar, failed to comply with the MVSFA or the Georgia Commercial Code, it could not assert a claim against Debtor's estate since it had no claim under state law, and therefore there was nothing to elevate in priority under § 507(b). The Bankruptcy Court rejected this argument and stated that Respondent was entitled to a claim equal to the alleged decrease in value between the date of the bankruptcy filing and the date of repossession, after application of adequate protection payments made.[5] Despite its statement of the formula for determination of a priority claim under § 507(b), the Bankruptcy Court based its award on the amount that Respondent paid to Paccar under the recourse obligation, $370,915.96. (Appendix C, page 33a).

Petitioner appealed to the District Court and on January 31, 1992, the District Court entered an order affirming the Bankruptcy Court. The District Court held that the Bankruptcy Code and "federal equitable principles" created claims in favor of Respondent even if the claims otherwise did not exist under applicable substantive law. (Appendix B, page 20a). The District Court also ruled that the amount Respondent paid to Paccar pursuant to its recourse obligation was related to and corresponded with the amount of decrease in value of the collateral during the pendency of the case, a conclusion that was not made or considered by the Bankruptcy Court. (Appendix B, page 30a).

Petitioner then appealed to the Eleventh Circuit Court of Appeals. On May 20, 1993, the Court of Appeals entered an opinion affirming the District Court, albeit on entirely different grounds. The Court of Appeals held that § 507(b) of the

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[5] The Bankruptcy Court's ruling was dependent upon a determination of the value of the collateral as of the date of the bankruptcy filing. However, no evidence of such value was presented. The only thing that Respondent established was the blue book value of trucks in ideal condition. There was no evidence whatsoever as to the actual condition of the collateral in question, as Respondent presented no witnesses that had actually seen the vehicles at the time of filing. This evidentiary failure did not stop the Bankruptcy Court from ruling in Respondent's favor, however.

Bankruptcy Code converts a creditor's claim to a superpriority claim in the event there is a failure of adequate protection. More importantly, the Court held that state law or other applicable non-bankruptcy law was utterly irrelevant to the issue of whether or not there was a claim that could be converted to an administrative expense priority under § 507(b) of the Bankruptcy Code. According to the Court, the Debtor's use of its own property postpetition created an independent claim in favor of Respondent separate and apart from the claim that Respondent was barred from asserting against the Debtor under state law. (Appendix A, page 5a).

Petitioner sought rehearing and rehearing *en banc*, and on September 30, 1993, the Court of Appeals denied Petitioner's request. The Court of Appeals rejected Petitioner's argument that the award of an administrative expense priority to a prepetition secured creditor ran afoul of the prohibition provided in § 361(3) of the Bankruptcy Code. The Court reiterated in its opinion that state law was utterly irrelevant to the determination of the existence and amount of a claim entitled to § 507(b) priority. (Appendix D, page 37a).

REASONS FOR GRANTING THE WRIT

The Supreme Court should hear this case because it involves important issues of federal bankruptcy law and its relationship to state law. The Court of Appeals' ruling that the Bankruptcy Code creates substantive claims between a debtor and his prepetition creditors without regard to state law reflects a fundamental misinterpretation of the purpose of bankruptcy. The Bankruptcy Code was not designed to supplant state substantive law; rather, the Bankruptcy Code was designed to operate as a statutory framework for the orderly administration and payment, either through reorganization or liquidation, of claims that are created under state law. The Court of Appeals has altered this framework in a fundamental way, thereby disrupting federal-state comity. The Bankruptcy Code is being used to usurp the role of state law in the *creation* of claims between a debtor and creditor. "Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such

interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.'" *Butner v. United States*, 440 U.S. 48, 55, 99 S. Ct. 914, 59 L. Ed. 2d, 136, 142 (1979).

The impact of the Court of Appeals' opinion is far reaching. The decisions' impact will be felt in bankruptcy cases across the county. The Bankruptcy Code can now be used as a sword by which secured creditors can gain an advantage over other creditors. What the Court of Appeals has done is use the Bankruptcy Code to create a claim under federal law in favor of a prepetition secured creditor whose claim is barred under state law. The claim then is given a superpriority, meaning that it is to be paid before any other claims are paid.[6] The Court of Appeals' opinion fundamentally changes the debtor-creditor relationship without any statutory basis.

The case is also important because it presents significant issues regarding the goal and purpose of adequate protection. The Bankruptcy Code specifically provides that prepetition secured creditors can exercise their rights against collateral if the automatic stay of § 362 of the Bankruptcy Code is lifted. The debtor can stop a court from lifting the stay if it can provide adequate protection to the creditor. The Court of Appeals has turned the concept of adequate protection on its head in this case. Rather than viewing adequate protection as merely the threshold requirement that the debtor must establish in order to continue the stay, the Court has determined that it is an entirely new claim independent and separate from the party's claims created under applicable state law.

This case involves important issues of statutory construction. The Bankruptcy Code specifically prohibits the use of an administrative expense priority as adequate protection. The Court of Appeals in this case, however, has ignored this prohibition. The

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[6] In this case, the result is that Chapter 11 administrative expense claimants will not be paid in full. Prepetition priority claimants such as the Internal Revenue Service will receive nothing.

decision of the Court of Appeals is in direct conflict with the express statutory language, thereby mandating reversal.

Section 507(b) of the Bankruptcy Code does not preempt state law so as to create an administrative expense claim in favor of a prepetition secured creditor whose claim is barred under state law.

The decision of the Court of Appeals renders state law irrelevant to the existence of Respondent's superpriority claim. As stated by the Court of Appeals:

> "Consequently, the Bankruptcy Court and the District Court correctly held that compliance with state law is irrelevant to the allowance of a claim for administrative expenses under § 507(b)." (Appendix A, page 37a).

The Court of Appeals' decision completely misconstrues the purpose of the Bankruptcy Code and its relationship to state law. The Bankruptcy Code is essentially a prioritizing scheme. It is not intended to supplant state or other applicable substantive law. Claims against a bankruptcy estate are created and determined under state law.[7] Respondent's claim against the Debtor arose because Respondent[8] advanced funding to the Debtor and took a security interest in twenty-six different vehicles as collateral. The substantive rights between Debtor and Respondent were governed by state law and the loan documents executed by the parties.

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[7] As used herein, the term "state law" will refer to the laws of the individual states as well as to other applicable substantive non-bankruptcy laws, all in accordance with the meaning of the term set forth in *Grogan v. Garner*, 498 U.S. 279, 112 L.Ed. 2d 755, 763 (1991).

[8] Because Respondent asserts rights as an assignee of Paccar's claim, the use of the term Respondent from this point forward will include Paccar.

Upon filing the bankruptcy, Respondent's ability to exercise its rights against the Debtor's property in which it held a security interest were stayed on account of § 362 of the Bankruptcy Code. In order to exercise its rights under state law, Respondent needed relief from the automatic stay. Relief is to be granted to a prepetition secured creditor unless the debtor provides adequate protection. Section 361 of the Bankruptcy Code provides that adequate protection can take many shapes, but specifically prohibits the granting of an administrative expense priority as adequate protection. One form of adequate protection authorized by § 361 of the Bankruptcy Code is the making of periodic payments such as was done in this case. The Code contemplates that a creditor will be diligent in its monitoring of the case. *In re Falwell Excavating Co., Inc.*, 47 Bankr. 217 (Bankr. W.D.Va. 1985). If the debtor fails to continue adequately protecting the creditor's interest in the collateral, the creditor must move in order to exercise its rights.

Once the automatic stay is lifted, the parties' rights revert to those under state law. *In re Kahihikolo*, 807 F.2d 1540 (11th Cir. 1987); *Matter of Winslow*, 39 Bankr. 869 (Bankr. N.D.Ga. 1984). Once the stay was lifted in this case, Respondent's rights were governed by the law of Georgia. By failing to timely comply with the provisions of Georgia's Motor Vehicle Sales Finance Act ("MVSFA"), which is codified at O.C.G.A. § 10-1-36, Respondent lost all rights to a deficiency claim[9] against the debtor or the estate.[10] *Davis v. Ford Motor Credit Company*, 164 Ga.App. 137, 296 S.E.2d 431 (1982). There is no dispute that Respondent failed to comply with the MVSFA. Such a failure is indisputedly fatal to Respondent's claim for the difference between the total debt and the

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[9] When a creditor's rights to a deficiency are barred, the creditor cannot assert its claim against any property of a debtor that was not granted as security for the debt. *Redmond Industries, Inc. v. Tower Properties, Inc.*, 517 F.Supp. 144 (N.D.Ga. 1981).

[10] Under § 558 of the Bankruptcy Code, the estate has the benefit of any defenses that would be available to the debtor as against any entity.

amount realized from the sale of the collateral.[11] *Bryant International, Inc. v. Crane*, 188 Ga. App. 736, 374 S.E. 2d 228 (1988). Thus, under Georgia law, Respondent could satisfy its claim only out of its collateral. Respondent could not satisfy its claim out of any other property or assets of the Debtor.

Despite the failure to comply with state law, Respondent in this case was awarded a claim against the estate under § 507(b), which provides:

> "If a [debtor-in-possession] provides adequate protection of the interest of a holder of a claim secured by a lien on property of the debtor and if, notwithstanding such protection, such creditor has a claim allowable [as an administrative expense under § 503(b)] arising from the stay of action against such property under § 362 of this title, from the use, sale, or lease of such property under § 363 of this title, or from the granting of a lien under § 364(d) of this title, then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection."

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[11] Respondent also failed to comply with the Commercial Code as adopted in Georgia. Respondent's failure to establish a commercially reasonable sale as required by O.C.G.A. § 11-9-504(3) created a rebuttable presumption that the collateral's value equalled the debt. *Emmons v. Burkett*, 256 Ga. 855, 353 S.E.2d 908 (1987). That presumption was not overcome here. The only way to overcome the presumption that the collateral's value equals the debt is to establish that the true value of the collateral was obtained at the sale. *Farmer's Bank v. Hubbard*, 247 Ga. 431, 276, S.E.2d 622 (1981). There was no evidence of value presented in this case other than the amount obtained in the unadvertised sale to Arrow Truck Center, Inc., and such sale price is insufficient as a matter of law to establish the actual value.

By the very language of the statute, in order to have a § 507(b) priority a creditor must first establish entitlement to an administrative expense claim under § 503(b) of the Bankruptcy Code.[12] As will be shown, a prepetition secured claim is not entitled to such a claim. What the Court of Appeals ruled in this case, however, was that § 507(b) created a claim for an administrative expense under § 503(b) in favor of a prepetition secured creditor in the event adequate protection fails. The Court of Appeals has it backwards. Section 507 does not create a claim upon a failure of adequate protection; rather, it simply prioritizes a claim that otherwise exists when there is a failure of adequate protection. The claim must exist independent of § 507(b).

In this case, Respondent's claim against the estate arose under its prepetition notes with the Debtor. The trucks were the property of the Debtor, but Respondent had a security interest in those trucks as security for the debt evidenced by the notes. The liability to Respondent by the Debtor did not arise on account of the use of the collateral - it arose on account of an advance of the purchase money. Because the Debtor's liability was based on the notes and not on the use of the collateral, the Debtor's postpetition retention of its own property did not give rise to an independent claim for the "actual, necessary costs and expenses of preserving the estate" as required in order for a creditor to receive a § 503(b) administrative expense. *In re Advisory Information and Management Systems, Inc.*, 50 Bankr. 627 (Bankr. M.D.Tenn.

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[12] Section 503(b) of the Bankruptcy Code provides that the "actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case," are administrative expenses.

1985). Since Respondent had no § 503(b) administrative claim, there was nothing to be given priority under § 507(b).[13]

The Court of Appeals has basically determined that the filing of a bankruptcy case converts a prepetition creditor's secured claim into two separate claims: one under state law arising under the loan documents and one under the Bankruptcy Code. According to the Court of Appeals, the retention of collateral by a debtor after a bankruptcy filing results in a claim that is independent of the claim under the state law. The satisfaction or extinguishment of the state law claim would have no effect on the claim under the Bankruptcy Code. This holding is in direct contrast to the notion espoused in the *Butner* decision that claims should be treated the same in federal and state courts. The Court of Appeals has given Respondent a claim greater than that available under state law by reason of the "happenstance of bankruptcy."

Respondent has implicitly recognized that state law is not irrelevant. In its motion for allowance of an administrative expense, Respondent specifically placed a cap on its administrative expense claim, and that cap was the amount of Respondent's unsecured claim against the estate.[14] Because there is no allowable unsecured claim against the estate in favor of Respondent in this case as a result of Respondent's failure to comply with the MVSFA and the Commercial Code, the cap recognized by Respondent in its motion operates to bar any § 507(b) priority. Such a cap is consistent with the notion that § 507(b) is designed to make a creditor "whole" if there is a failure of adequate protection. A creditor is "whole" if it receives everything it is entitled to under its loan documents and

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[13] Reliance by the Court of Appeals on *Grundy National Bank v. Rife*, 876 F.2d 361, 363 (4th Cir. 1989) to support its holding is misplaced. In *Grundy*, there was no question of the existence of the claim. The Court in *Grundy* merely held that a claim can be elevated to a superpriority if there is a failure of adequate protection. The issue in this case is whether § 507(b) of the Bankruptcy Code creates a claim where applicable state law specifically bars it.

[14] In its motion, Respondent asserted that the collateral diminished in value by $465,861.40, but that the administrative expense claim was limited to the total unsecured claim of $413,561.71.

state law. The cap ensures that such a creditor does not receive more.

The relationship between state law and the priority available to an administrative expense claimant under § 507(b) of the Bankruptcy Code can be illustrated by the case *In re James B. Downing & Co.*, 94 Bankr. 515 (Bankr. N.D.Ill. 1988). In that case, the Bankruptcy Court denied § 507(b) priority to a prepetition secured creditor because that creditor had advanced no postpetition costs or expenses or new credit to preserve the estate. Thus, the *James B. Downing* decision recognized that § 507(b) did not create a claim, and further recognized that a prepetition secured creditor did not become entitled to an administrative expense claim simply because the debtor retained collateral postpetition. Additionally, the *James B. Downing* case recognized that a pre-petition secured creditor's claim, if any, to an administrative expense priority under § 507(b) of the Bankruptcy Code is necessarily limited to the pre-petition secured creditor's claim against the estate. According to the *James B. Downing* court, a superpriority is only available, if at all, to the extent that a creditor's unsecured *deficiency* claim against an estate has increased during the pendency of the case. Obviously, if there is no unsecured deficiency claim against the estate, then there is no increase in that claim from which a § 507(b) priority can arise. Since Respondent in this case has no unsecured deficiency claim against the estate by virtue of Respondent's failure to comply with Georgia law, there is no increase in an unsecured deficiency which can be given additional priority under § 507(b).

Clearly, state law is not irrelevant to the creation and existence of a prepetition secured creditor's claim with priority under § 507(b) of the Bankruptcy Code. To hold otherwise is to transform the Bankruptcy Code from a prioritizing scheme into a scheme that creates and governs the substantive rights between the parties. That was not what the Bankruptcy Code was designed to do. In this case the result is that Respondent will receive more than it was entitled to under state law. The Court of Appeals has used the Code to usurp state law, a result that cannot be upheld.

The award of an administrative expense priority to a prepetition secured creditor is in direct conflict with the plain meaning of § 361(3).

The Court of Appeals held that § 507(b) of the Bankruptcy Code creates in favor of a prepetition secured creditor an administrative expense priority. According to the Court, a debtor's retention of collateral in which a creditor has a security interest creates a claim in favor of that creditor independent from the claim under the note secured by the collateral. This ruling emasculates the prohibition contained in § 361(3) of the Bankruptcy Code against granting an administrative expense priority as adequate protection.

The Bankruptcy Code provides a very specific procedure for the treatment of secured claims. As shown previously, a secured creditor's rights as against a debtor and the debtor's property are determined by reference to state law and the loan documents between the parties. The filing of a bankruptcy does not dispose of the loan documents; rather, it merely stays enforcement of the provisions of those documents that authorize the creditor to foreclose upon collateral in the event of default. The stay is automatic and arises immediately from the commencement of the case. § 362 of the Bankruptcy Code. In order for a prepetition secured creditor to exercise its state law rights with respect to its collateral, it must obtain relief from the automatic stay. Under § 362(d) of the Bankruptcy Code, relief from the stay is to be granted unless adequate protection is provided. The remedy available to a prepetition secured creditor that is not adequately protected is relief from the automatic stay in order to exercise its state law rights.[15]

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[15] The Bankruptcy Code provides an expedited procedure for obtaining relief from the stay. If a creditor files a motion to lift the automatic stay and the matter is not heard within thirty days of the date of the motion, the stay is automatically lifted with respect to an act against property of the bankruptcy estate. 11 U.S.C. § 362. Even without a hearing, the Court may grant relief from the stay in order to prevent irreparable damage to the interest of an entity in property. 11 U.S.C. § 362(f).

In order to avoid stay relief, a debtor must provide adequate protection. That concept is given meaning in § 361 of the Bankruptcy Code. Adequate protection may be provided by three different means: (1) the making of cash or periodic cash payments; (2) the providing of an additional or replacement lien; or (3) the providing of other relief as will result in the realization by the moving party of the indubitable equivalent of the moving party's interest in the property, *other than granting of compensation allowable as an administrative expense under § 503(b)(1) of the Code*. Thus, the statute specifying the types of adequate protection that may be allowed to a prepetition secured creditor specifically prohibits the award of an administrative expense priority as adequate protection. *In re Smith*, 75 Bankr. 365, 368 (W.D.Va. 1987).

The Bankruptcy Code therefore treats prepetition secured creditors in a certain way. The creditors are allowed to exercise their state law rights with respect to their collateral unless adequate protection is provided. Adequate protection cannot be in the form of an administrative expense priority. Therefore, the Bankruptcy Code specifically prohibits a prepetition secured creditor such as Respondent being awarded an administrative expense priority for the debtor's postpetition retention of property owned by the debtor in which the creditor asserts a security interest. *In re Advisory Information & Management Systems, Inc.*, *supra* at 629. ("We do not believe § 503(b) is intended to provide an administrative expense award to a prepetition secured lender based on the debtor's postpetition possession and use of collateral....As an ordinary prepetition secured party [the creditor] is only entitled to the usual remedies as a secured lender in a bankruptcy case - no more, no less.")

The problem with the analysis of the Court of Appeals is that it completely emasculates the prohibition of § 361(3) of the Bankruptcy Code. The Court of Appeals held that under § 507(b), Debtor's postpetition retention of collateral securing Respondent's prepetition claim gave rise to a postpetition claim in favor of Respondent that was converted into an administrative expense under § 507(b) on account of an alleged failure of adequate protection. In affect, the Court of Appeals has awarded Nalley, a prepetition

secured creditor, an administrative expense priority as adequate protection. This is prohibited by the express language of § 361(3).

The conflict between the Court of Appeals' § 507(b) analysis and the language of § 361(3) is underscored by an examination of the purpose and nature of administration expense priorities. Administrative expense claims are supposed to be claims for the "actual, necessary costs and expenses of preserving the estate." In order to have a claim allowable as an administrative expense under § 503(b) of the Bankruptcy Code, there must be a concrete benefit to the estate on account of the claim, and the claim must arise from a transaction with the postpetition debtor or trustee that is beneficial to the estate. *In re Subscription Television of Greater Atlanta*, 789 F.2d 1530 (11th Cir. 1986); *In re Advisory Information Management Systems, Inc., supra* at 629. ("We do not agree with the proposition that a secured creditor 'contributes' to the administration of an estate as contemplated by § 503(b) where the debtor-in-possession merely continues using property which the pre-petition debtor owned."). The Court of Appeals has provided a prepetition secured creditor with a claim that is only available to postpetition providers of goods and services. This is contrary to the scheme of the Bankruptcy Code. The result is that those creditors that provided new credit and new goods or services to the debtor-in-possession are being subordinated to a prepetition secured creditor who did not provide any new credit or new goods or services to the estate. This is contrary to the Bankruptcy Code's scheme of giving a priority to people that advance new products or credit to a debtor-in-possession as an incentive to do business with the debtor-in-possession.

Ignoring the prohibition of § 361(3) wreaks havoc on the priority scheme of the Bankruptcy Code. Section 507 of the Bankruptcy Code sets forth the order of priority of valid claims when funds are insufficient to pay all such claims in full. "Priorities are designed to assure payment, if possible, to certain classes of claims by requiring that they be first paid before others are satisfied." 3 *Collier on Bankruptcy*, § 507.02, p. 507-9 (15th Ed. 1991). Priorities are to be strictly construed. It is an important policy of the Bankruptcy Code that creditors within a given class be treated equally, and that bankruptcy courts not create their own superpriorities within a single class. *Shapiro v. Saybrook (In re*

Saybrook Manufacturing Co., Inc.), 963 F.2d 1490, 1495-6 (11th Cir. 1992). The limited resource of a debtor ought to be distributed equally and fairly among creditors, and that is why statutory priorities are to be narrowly construed. If a creditor does not establish entitlement under one of the specific priority statutes, such creditor is not entitled to a priority. *Joint Industry Board of the Electrical Industries v. United States*, 391 U.S. 224, 228, 88 S. Ct. 1491, 1493 (1968). In this case, Respondent is being favored over other prepetition secured creditors, as well as over those creditors that advanced new goods, services, or credit to the debtor postpetition. In order for Respondent to be entitled to such preferential treatment, Respondent must establish entitlement under the specific language of the Bankruptcy Code. That is where Respondent failed. The Bankruptcy Code does not authorize an award of an administrative expense priority to a prepetition secured creditor. In fact, it prohibits it.

The Court of Appeals recognized that the language of § 361(3) conflicts with the result in this case but attempted to avoid that conflict by referring to the legislative history. According to the Court of Appeals, the legislative history reinforces the construction that although there is an "*ex ante* prohibition on the use of an administrative expense claim, it is specifically allowed as a remedy for the later failure of the adequate protection granted." (Appendix D, page 36a). The main problem with the Court of Appeals' analysis is, of course, the plain language of the statute. The starting point for analysis of any statute is the language of the statute, and that is where the analysis ends in this case since the language is plain. *United States v. Ron Pair Enterprises*, 489 U.S. 235, 241, 109 S. Ct. 1026, 103 L. Ed. 2d 290, 298 (1989). The Court of Appeals, however, ignored the plain language of the statute and limited the express prohibition of § 361(3) to the awarding of adequate protection in the first instance. (Appendix D, page 36a). Section 361 does not contain such a limitation. It simply provides that where adequate protection is required, such adequate protection may be provided by different ways except the granting of an administrative expense claim.

The Court of Appeals' decision to disregard the plain language of § 361(3) runs counter to the policy underlying the

Bankruptcy Code. The dominant theme of the Bankruptcy Code is equality of distribution among creditors. *In re Cascade Oil Co., Inc.*, 51 Bankr. 877 (Bankr. D.Kan. 1985). The presumption of bankruptcy is that the limited resources of a debtor will be equally distributed among creditors. *Trustees of the Almalgamated Insurance Fund v. McFarlins, Inc.*, 789 F.2d 98, 100 (2nd Cir. 1986). By awarding Respondent a superpriority in this case, the Court of Appeals has done violence to the theme of equality of distribution. Respondent is being favored over other creditors, including those creditors similarly situated. More importantly, Respondent is being favored over creditors who actually complied with the provisions of the MVFSA and the Georgia Commercial Code. Many of the prepetition secured creditors obtained relief from the stay and foreclosed on their collateral, complying with Georgia law in the process. That compliance with Georgia law gave those creditors an unsecured claim against the estate. The Court of Appeals in this case has taken the one creditor that did not comply with Georgia law and given it priority over all other creditors. This result cannot be tolerated.

The Supreme Court decision *Vanston Bondholders Protective Committee v. Green*, 329 U.S. 156, 67 S. Ct. 237 (1946) provides an illustration of the policy of equality of distribution. In that case, the Supreme Court faced the issue of whether or not bondholders should be paid interest on interest with regard to their claims against the estate of a debtor. The Court first *assumed* that such interest was allowable under applicable state law. The Court then addressed whether allowance of the claim in question was compatible with the policy of bankruptcy. Because the primary principle governing bankruptcy was equality of distribution, and because allowing interest on interest would enrich the bondholders to the harm and detriment of subordinate creditors, the Supreme Court held that equality of distribution militated in favor of disallowing the claim. In other words, even assuming that the claim was valid under state

law, the Court still disallowed it in order to promote the fundamental goal of bankruptcy.[16]

The Court of Appeals' disregard for the plain language of § 361(3) violates Georgia's public policy. This is further evidence that § 361(3) should be enforced according to its terms. Georgia's public policy is reflected in its antideficiency statutes such as the MVSFA and the Commercial Code, both of which are designed to protect against a creditor buying a property at foreclosure for less than its actual value. "Indeed, [antideficiency] statutes are thought necessary to prevent inequities that arise when a creditor buys property on which it has foreclosed at a low price when property values are depressed and the economy is recessionary, and then proceeds to seek a personal judgment against the debtor for the difference between the low price the creditor paid for the property at the foreclosure sale and the balance of the debt." *Redmond Industries v. Tower Properties, Inc.*, 517 F.Supp. 144 (N.D.Ga. 1981). The antideficiency statutes do not just protect the debtor, they also protect other creditors. Enforcement of the antideficiency statutes maximizes the assets that might be available for satisfaction of creditor claims. This public policy is particularly important in the bankruptcy context. A creditor that fails to comply with Georgia law following repossession and foreclosure is barred from seeking to satisfy its claim out of other assets of a debtor. Those assets are then available for creditors who do not have the benefits of security. Antideficiency statutes promote the fundamental principal of bankruptcy - equality of distribution.

The Bankruptcy Code expressly contemplates the use of antideficiency statutes to prohibit a creditor from receiving a

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[16] The *Vanston* decision was the cornerstone of the District Court's order in this case. (Appendix B, p. 19a). The District Court interpreted *Vanston* as standing for the proposition that bankruptcy courts can create claims under "federal equitable principles" irrespective of whether those claims exist under state law. Ironically, the District Court was using *Vanston* to *allow* a claim that did not exist under state law. The District Court simply took the *Vanston* decision and turned it on its head. Despite being the cornerstone of the District Court decision and Respondent's arguments, the *Vanston* decision was never mentioned by the Court of Appeals.

windfall. Section 502(b)(1) provides that a claim against the estate is disallowed to the extent that the claim is unenforceable against the debtor for any reason other than because the claim is contingent or unmatured. The entire purpose of this statute is to enable debtors or trustees to enforce antideficiency statutes or nonrecourse obligations in bankruptcy. *See, generally*, 3 *Collier on Bankruptcy*, § 502.02, p. 502-29 (15th Ed. 1991).

Respondent has asserted that the prohibition of § 502 applies only to prepetition claims, not to *postpetition* claims like the claim that Respondent has in this case. Of course, the prohibition has to apply to Respondent's claim since Respondent's claim arose under the notes that Debtor executed in favor of Respondent, and that claim was distinctly a prepetition claim. In any event, this argument completely ignores § 558 of the Bankruptcy Code. That section gives the estate the benefit of any defense available to the debtor as against any entity other than the estate, including statutes of limitation, fraud, usury, and other personal defenses. "Section 558, as with its predecessors, deals with all the debtor's defenses, affirmative as well as negative. It provides the trustee with every defensive weapon available to the debtor. The personal character of a particular defense under state or federal law is immaterial." 4 *Collier on Bankruptcy*, § 558.01, p. 558-4 (15th Ed. 1991). Thus, even if § 502(b)(2) is limited to prepetition claims, § 558 can be relied upon by the Trustee or the estate in order to defeat a claim, whether prepetition or postpetition.

The award of an administrative priority claim to a prepetition secured creditor is in direct conflict with the express language of § 361(3). The public policy behind the federal Bankruptcy Code and the public policy behind Georgia's antideficiency statutes are both violated by the Court of Appeals' disregard of § 361(3). Reversal is mandated.

CONCLUSION

Substantive claims are created in commercial transactions by state law. The Bankruptcy Code was not designed to and does not create such claims. The Bankruptcy Code was designed to prioritize claims that otherwise exist. The Court of Appeals made a

fundamental error when it held that the Bankruptcy Code created a claim that was separate and distinct from the state law claim that existed between the parties. The claim that Respondent had against the estate was not created by § 507(b) of the Bankruptcy Code; it arose from the obligation under state law to pay the installment notes that were executed prepetition. Because Respondent failed to comply with Georgia law following repossession, it was barred from asserting any claim against any property other than the collateral. The existence of bankruptcy did not change that result. The Court of Appeals is using the Bankruptcy Code to create a claim that could not exist under substantive state law.

The creation of the claim by the Court of Appeals is in direct violation of the statutory language of the Bankruptcy Code. Section 507(b) provides that a claim for an administrative expense priority will be given a superpriority over other administrative expenses if adequate protection was provided and if, despite such adequate protection, the creditor has a claim for an administrative expense arising from the stay of action against property. Thus, before the superpriority kicks in, the creditor must establish entitlement to an administrative expense, a remedy not available to a prepetition secured creditor such as Respondent. The mere retention by the Debtor of its own property postpetition did not create an administrative expense claim in favor of Respondent. To hold otherwise is to provide an administrative expense priority as adequate protection, which is prohibited under the plain language of § 361(3).

The award also violates the statutory scheme of bankruptcy. The existence of a claim held by a prepetition secured creditor is a matter of state law. If a debtor defaults under secured notes, the creditor is entitled to exercise its state law rights with respect to the collateral. All that a bankruptcy does is stay a creditor's collection activity, whether through foreclosure on its collateral or otherwise. A prepetition secured creditor's remedy is not an administrative expense priority. Those priorities are designed to protect creditors that advance new credit and new products to a debtor or estate post-filing, not to a prepetition secured creditor. Respondent's remedy was to obtain relief from the stay and foreclose on its collateral. Respondent did that, it failed to comply with applicable Georgia

law, and it therefore lost any additional right to assert a claim against assets other than its collateral.

Not only is the statutory scheme of the Bankruptcy Code undermined by the award to Respondent in this case, but the very policy of equality of distribution is violated. Additionally, the Georgia public policy of protecting both debtors and creditors through antideficiency statutes is violated. The Bankruptcy Code was not designed to violate the public policies of the individual states. The decision in this case does just that.

For the reasons stated herein, a writ of certiorari should be issued to review the judgment and opinion of the Eleventh Circuit Court of Appeals.

Respectfully submitted.

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December 27, 1993

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
ELEVENTH CIRCUIT

No. 92-8223

PAUL W. BONAPFEL, AS TRUSTEE
FOR THE ESTATE OF
CARPET CENTER LEASING COMPANY, INC.
Plaintiff-Appellant

v.

NALLEY MOTOR TRUCKS, A DIVISION OF
NALLEY CHEVROLET, PACCAR FINANCIAL CORP.
Defendants-Appellees

Appeal from the United States District Court
for the Northern District of Georgia

[Entered May 20, 1993]

Before KRAVITCH and ANDERSON, Circuit Judges, and HILL, Senior Circuit Judge.

Paul W. Bonapfel, Trustee for Carpet Center Leasing Co., Inc., appeals the District Court's order affirming the Bankruptcy Court's judgment granting Nalley Motor Trucks' claim for administrative expense priority in the amount of $370,915.96 pursuant to § 507(b) of the Bankruptcy Code. Appellant contends

that the judgment is erroneous because the creditor is not entitled to an administrative expense claim. We conclude that the District Court properly affirmed the Bankruptcy Court, and therefore affirm.

I. BACKGROUND

This case involves proceedings surrounding the bankruptcy case of Carpet Center Leasing Co., Inc. ("Debtor"). When Debtor filed for bankruptcy under Chapter 11 on February 25, 1987, it operated a large fleet of tractors and trailers, including twenty six tractors in which Paccar Financial Corporation ("Paccar") held a security interest. Pursuant to a consent decree between Debtor and Paccar, Debtor was allowed to continue using the twenty six tractors in bankruptcy in exchange for monthly "adequate protection" payments to Paccar to protect Paccar's interest in the depreciating collateral. These adequate protection payments were roughly half of the total monthly payments due under the original installment purchase contracts between Debtor and Paccar. Over a nine month period, Debtor paid a total of $108,500 to Paccar in adequate protection payments pursuant to the consent order, although some of the payments were not timely.[1]

On March 3, 1988 Paul W. Bonapfel, appellant herein, was appointed Trustee of Debtor's bankruptcy estate. Because Debtor had not made timely adequate protection payments, the Trustee and Paccar entered a consent order on March 3, 1988 which lifted the automatic stay and allowed Paccar to foreclose on the tractors. The consent order was entered without prejudice to Paccar's right to assert any other claims it might have against the Debtor's estate. Paccar repossessed most of its collateral during March and April of 1988. On August 19, 1988 Paccar conducted a public foreclosure sale at which Paccar was the only bidder and it bought the tractors

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[1] During the course of these payments, Debtor paid in full three of the ten installment contracts. The number of tractors covered by the security interest was reduced from twenty six to twenty three, and the monthly adequate protection payments were reduced pro rata.

for $89,000. Two months later, and six months after the stay was lifted, Paccar sold the trucks by private sale to Arrow Truck Center, Inc. ("Arrow") for $60,000.

On March 30, 1988 the Trustee filed a motion to convert the case from Chapter 11 to Chapter 7, and this motion was granted by the Bankruptcy Court on May 17, 1988. On October 14, 1988 Paccar filed a motion asserting a claim for administrative expenses amounting to $413,561.71, plus interest and fees.[2] Pursuant to a recourse obligation, Nalley Motor Trucks ("Nalley"), Appellee herein, paid Paccar $370,915.96 and was assigned all of Paccar's claims against the Debtor as successor-in-interest. Nalley was subsequently substituted for Paccar in the bankruptcy case on February 12, 1990.

At trial, Nalley presented expert testimony that the "Blue Book" value of the tractors on the date of bankruptcy filing was about $575,000. Nalley's expert had not personally inspected the vehicles, but he relied on photographs and business records compiled during inspections of the vehicles at the time of repossession. Nalley alleged that the $60,000 received from the private sale represented the fair market value of the vehicles at the time of repossession because, by then, all but two of the repossessed vehicles were salvage value only. The Trustee contended that the vehicles had a retail resale value of $425,873. The Bankruptcy Court agreed with Nalley.

The Bankruptcy Court awarded $370,915.96 to Nalley as an administrative expense priority pursuant to § 507(b) of the Bankruptcy Code for the diminution in value of the collateral that occurred because of Debtor's continued use of the trucks pursuant to the automatic stay in bankruptcy. This award equalled the sum

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[2] Apparently, Paccar based its administrative expense claim on the diminution in value of the collateral, but limited the amount to the deficiency on the installment purchase contracts. Thus, the sum claimed equals the amount due under these contracts.

that Nalley paid Paccar on its recourse obligation. The District Court affirmed this award.

II. DISCUSSION

A. Nature of Claim

[1] At the outset, we must clarify the nature of Nalley's claim in order to focus on the issues actually involved in this case. The Trustee argued both in his briefs and at oral argument that Nalley's claim is barred by Paccar's alleged failure to comply with foreclosure laws of the State of Georgia. The Trustee contends that because Paccar failed to carry out foreclosure and sale of the collateral according to the terms of the Georgia Motor Vehicle Sales Finance Act and the Georgia Commercial Code, Nalley, as successor-in-interest, cannot assert a claim against Debtor's estate based on the loss suffered by Paccar when the sale of the collateral produced less than the balance due on the purchase money notes.

This argument misses the point. A claim for administrative expenses under 11 U.S.C. § 507(b) is not a claim for a deficiency on the underlying obligation which financed Debtor's purchase of the collateral. The Trustee appears to be correct in asserting that compliance with state law controls a creditor's right to claim, against a bankruptcy estate, a deficiency on a contract after foreclosure of a lien. We need not reach that question, however, because this case does not present that issue. Instead of a contract deficiency claim, Nalley asserts a claim for administrative expenses for the value of goods furnished to the bankruptcy estate after imposition of the automatic stay. Section 507 of the Bankruptcy Code affords first priority to administrative expenses "to encourage the provision of goods and services to the estate, and to compensate those who expend new resources attempting to rehabilitate the estate." *In re Pulaski Highway Express, Inc.*, 57 B.R. 502, 505 (Bankr.M.D.Tenn.1986). Section 507(b) states:

> If the trustee, under section 362, 363, or 364 of this title, provides adequate

> protection of the interest of a holder of a claim secured by a lien on property of the debtor and if, notwithstanding such protection, such creditor has a claim allowable under subsection (a)(1) of this section arising from the stay of action against such property under section 362 of this title, from the use, sale, or lease of such property under section 363 of this title, or from the granting of a lien under section 364(d) of this title, then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection.

11 U.S.C. § 507(b). This section provides that when adequate protection has been given to a secured creditor and later proves to be inadequate, the creditor becomes entitled to a superpriority administrative expense claim to the extent that the proffered adequate protection was insufficient. *Grundy Nat'l Bank v. Rife*, 876 F.2d 361, 363 (4th Cir. 1989); *In re James B. Downing & Co.*, 94 B.R. 515, 520 (Bankr. N.D.Ill. 1988); *In re McGill*, 78 B.R. 777, 779 (Bankr. D.S.C. 1986); *In re Mutschler*, 45 B.R. 494, 496 (Bankr. D.N.D. 1984), *aff'd Grundy Nat'l Bank v. Rife*, 102 B.R. 57 (Bankr. W.D.Va. 1987); *In re Callister*, 15 B.R. 521, 528 (Bankr. D.Utah 1981). Administrative expenses are governed by § 503(b) of the Bankruptcy Code, which provides, in part, that administrative expenses include "the actual, necessary costs and expenses of preserving the estate." 11 U.S.C. § 503(b)(1)(A).

[2] Within the scheme of the Bankruptcy Code, § 507(b) "converts a creditor's claim where there has been a diminution in the value of a creditor's secured collateral by reason of a § 362 stay into an allowable administrative expense claim under § 503(b)." *Grundy Nat'l Bank*, 876 F.2d at 363-4. Accordingly, the question of whether Nalley could pursue a deficiency claim on the installment

purchase contracts under the laws of Georgia is irrelevant to the central issue of this case which is whether Nalley was entitled to recover administrative expenses under section 507(b) of the Bankruptcy Code. This administrative expense claim is based on the insufficiency of adequate protection in covering the post-petition diminution in value of the trucks furnished by Paccar and used by the estate. Under *Grundy Nat'l Bank*, this is a separate claim from a deficiency claim.

B. Entitlement to Administrative Expense Claim

1. Benefit to Bankruptcy Estate

[3] In addition to contending that Nalley's claim is barred by failure to comply with state law, the Trustee also raises several arguments alleging that Nalley failed to establish a valid administrative expense claim. First, the Trustee argues that a pre-petition secured creditor cannot elevate his claim to a super-priority administrative expense claim just because the debtor used the property post-petition and adequate protection proved to be inadequate. The Trustee insists that in order for a claim to qualify as an "actual, necessary cost and expense of preserving the estate" under 11 U.S.C. § 503(b), the creditor must establish that there has been an actual, concrete benefit to the estate on account of a transaction with the debtor which is beneficial to the estate. App. Br. at 44-46, citing *In re Subscription Television*, 789 F.2d 1530 (11th Cir. 1986); *In re James B. Downing & Co., supra*; *In re Jartran, Inc.*, 732 F.2d 584 (7th Cir. 1984); and *In re Advisory Info. and Management Sys., Inc.*, 50 B.R. 627 (Bankr. M.D.Tenn. 1985). The Trustee alleges further that mere continued use of collateral by a debtor-in-possession is not enough to establish an administrative expense claim because such a claim requires the advancement of goods or services pursuant to a post-petition transaction. Based on these principles, the Trustee argues that Nalley has only a deficiency claim on the installment contracts because its predecessor-in-interest, Paccar, did not provide any new value to the estate after the imposition of the automatic stay.

However, this case does involve a post-petition transaction beneficial to Debtor's estate rather than a mere continued use of the trucks by Debtor. Paccar consented to forgoing foreclosure on its secured collateral only after negotiating for adequate protection payments in return for leaving the trucks in Debtor's possession. Facing a similar claim of administrative expenses for failed adequate protection, the court in *In re Mutschler* stated:

> Section 503(b)(1)(A) of the Code entitles a creditor to administrative priority for any claim representing an actual and necessary cost of preserving the estate. Section 507(b) is an adjunct to the adequate protection alternative set forth in section 361. Section 507(b) simply provides that where adequate protection has been extended to a secured creditor and later proves to be inadequate, the creditor then becomes entitled to a superpriority administrative expense claim to the extent that the proffered adequate protection was insufficient. Adequate protection is a means of preserving a creditor's interest in secured collateral subject to post-petition use by the debtor. *Presumably such use is desired by the debtor and is contributing to the reorganization effort. Otherwise, the debtor would doubtless return the collateral and forgo providing adequate protection. This beneficial use by the debtor is normally "paid for" by the adequate protection.* Where adequate protection becomes inadequate or otherwise fails and the use nonetheless continues, section

> 507(b) comes into play by covering the creditor's unprotected interest by according it priority administrative expense status.

(emphasis added) 45 B.R. at 496; *accord In re McGill*, 78 B.R. at 780. (That the use of the collateral was necessary to the debtor's reorganization is evidenced by the debtor's efforts to retain the collateral by attempting to provide adequate protection payments).

[4] Here, as in *In re Mutschler* and *In re McGill*, Debtor actively sought to retain possession of the tractors by agreeing to pay Paccar monthly adequate protection payments. The negotiation for continued possession of the tractors in return for adequate protection is a post-petition transaction providing new value to the bankruptcy estate. Debtor's efforts to retain the tractors demonstrate that the collateral was beneficial to the estate. When a debtor-in-possession uses a creditor's equipment to generate funds for the operation of a business in bankruptcy, the creditor's expense of providing that equipment is an actual and necessary cost of preserving the bankruptcy estate under § 503(b). *In re CM Sys., Inc.*, 86 B.R. 286, 287 (Bankr. M.D.Fla. 1988). The Trustee has not argued that Debtor did not use the trucks while they were in Debtor's possession, so presumably the trucks were used to generate funds for the operation of Debtor's business. Thus, expenses incurred by Paccar in furnishing these trucks to the Debtor qualify as actual and necessary expenses of preserving the estate.

The cases relied upon by the Trustee are readily distinguishable from the case at bar. In *In re Jartran, Inc., supra*, the debtor enjoyed the benefits of advertising services that were performed on the basis of pre-petition contracts. The advertising service provider claimed entitlement to administrative priority for the cost of providing the ads, but the Seventh Circuit Court of Appeals held that the debtor engaged in no post-petition transaction which induced the provision of the ads because the commitment to provide the ads was formed before the debtor filed its bankruptcy petition. *In re Jartran, Inc.*, 732 F.2d at 588-89. In this case, by

contrast, Debtor induced the post-petition provision of goods to the estate by negotiating for retention of the trucks, otherwise subject to repossession, in return for adequate protection payments. Rather than simply enjoying the benefits of a pre-petition commitment, Debtor actively bargained for the use of the tractors after filing its bankruptcy petition.

In Advisory Information and Management Systems, supra, the Bankruptcy Court considered a claim for administrative expenses under section 503(b)(1)(A) by a creditor who allowed the debtor-in-possession to continue using the collateral without seeking adequate protection for one year after the bankruptcy petition was filed. After commenting that there is "nothing in § 503 remotely suggesting that administrative expense priority was intended as an optional remedy to adequate protection of a secured claimholder's interest in property of the estate," the court held that a secured creditor does not "contribute" to the administration of an estate by merely sitting back and allowing the debtor-in-possession to continue using property which the pre-petition debtor owned. *In re Advisory Info. and Management Sys., Inc.*, 50 B.R. at 630. Similarly, the Bankruptcy Court in *In re James B. Downing & Co., supra*, held that a creditor who did not seek adequate protection for its lien and who did not advance any post-petition costs or expenses to preserve the estate was not entitled to claim § 503 administrative expenses. 94 B.R. at 521.

[5] Unlike the creditors in *Advisory Information and Management Systems* and *James B. Downing*, Nalley's predecessor-in-interest utilized the statutory procedures provided for protection of its collateral in the possession of Debtor. Nalley does not proffer § 503 as an alternative to adequate protection of its secured claim. Instead of merely sitting back and allowing Debtor to continue using the tractors, Paccar asserted its undeniable right to repossession and agreed to forgo repossession only after and because Debtor consented to paying adequate protection. Therefore, Nalley's administrative expense claim is not barred under the

inaction theory which controlled in *Advisory Information and Management Systems* and *James B. Downing*.

[6] Finally, in *Subscription Television, supra*, this Court faced a situation where the debtor held a post-petition sixty day executory contract which obligated the creditor to provide the debtor with unscrambled television broadcast signals, but the debtor actually used the broadcast signals only seventeen days. The provider of the broadcast signals claimed a § 507 administrative expense priority for the entire sixty day period on the theory that it had been deprived of its own use of the television signals because the contract required it to keep the signals available to the debtor. This Court held:

> That which is actually utilized by a Trustee in the operation of a debtor's business is a necessary cost and expense of preserving the estate and should be accorded the priority of an administrative expense. That which is thought to have some potential benefit, in that it makes a business more likely salable, may be a benefit but is too speculative to be allowed as an "actual, necessary cost and expense of preserving the estate."

In re Subscription Television, 789 F.2d at 1532. Thus, this Court denied the creditor's administrative expense claim for the portion of the contract period wherein the debtor did not actually use the broadcast signals.

The debtor in the case at bar enjoyed more than mere potential post-petition use of collateral. Rather than entertaining a speculative benefit, the Trustee actively used Paccar's collateral throughout its post-petition possession. This is not disputed. The reasoning of *Subscription Television*, therefore, leads to the conclusion that Nalley is entitled to an administrative expense

priority because the Trustee actually used the collateral to the benefit of the debtor's estate. Because this case does not involve a debtor's potential use of collateral, the Trustee's reliance on *Subscription Television* is misplaced.

2. Increase in Deficiency Claim

[7] The second argument raised by Trustee to persuade this Court that Nalley failed to establish entitlement to an administrative expense claim is based on language from the *James B. Downing* case. The court in *James B. Downing* faced the question of whether the provision of adequate protection was a prerequisite to the grant of an administrative expense priority. In resolving this issue the court quoted a passage from Bankruptcy by Ginsberg which states in part:

> If the adequate protection given by the court proves to be inadequate, that is, the secured creditor winds up being injured from the continuation of the stay, use of the property, or funding the estate in the sense that its unsecured deficiency claim against the estate is increased, the creditor is entitled to a superpriority for the increase in the deficiency.

In re James B. Downing & Co., 94 B.R. at 521, *quoting* Ginsberg, Bankruptcy ¶ 10,705 (1986). The Trustee seizes upon this language as establishing that an administrative expense claim is based on the amount by which an unsecured deficiency claim increases by virtue of the automatic stay. Here, the Trustee maintains that Nalley had no unsecured deficiency claim because of Paccar's failure to comply with Georgia foreclosure laws, and accordingly no administrative expense claim could arise because there was no increase in an unsecured deficiency claim.

[8] The Trustee's argument fails to recognize the nature of an administrative expense claim. As described above, Nalley's administrative expense claim is distinct from the deficiency claim it might have perfected. Contrary to the implications of the dicta from *James B. Downing* relied upon by the Trustee, an administrative expense claim is based on the diminution in the value of the collateral by reason of the automatic 362 stay. *Grundy Nat'l Bank v. Rife*, 876 F.2d at 364; *see also In re Colter*, Inc., 53 B.R. 958, 961 (Bankr.D.Colo.1985) (Section 507(b) confers a superpriority administrative expense claim to the extent the creditor has suffered an actual decrease in the value of its interest in the collateral due to the automatic stay and the debtor's use of its collateral, less any adequate protection payments made by the debtor); *In re Becker*, 51 B.R. 975, 980 (Bankr.D.Minn.1985) (Actual loss sustained due to failure of adequate protection determines the amount allowed as a superpriority administrative expense under § 507(b)). Because Nalley's administrative expense claim arose from the deterioration in the value of the trucks rather than an increase in its deficiency claim on the sales contracts, the Trustee's argument cannot prevail.

3. Loss Attributable to Automatic Stay

[9] A third argument the Trustee makes in support of its contention that Nalley failed to establish an administrative expense claim is that Nalley failed to demonstrate that the loss in value of the collateral was attributable to the automatic stay. Relying on *In re Falwell Excavating Co., Inc.*, 47 B.R. 217 (Bankr.W.D.Va.1985), the Trustee asserts that when a creditor acquiesces to some harm to its collateral for business or other reasons, any alleged impairment of value may not be attributed solely to the automatic stay. The Trustee alleges that Nalley presented no evidence of any steps it took to preserve or protect its collateral or to require strict compliance on the part of the debtor.

In Falwell Excavating Co., the creditor had made a business decision to not enforce strict compliance with an adequate protection order for a period of over two years, although the adequate

protection payments, if made on time, would have protected the creditor from all of the diminution in value of the collateral. In this case, even if the debtor had made all of its adequate protection payments, Paccar still would have suffered an unprotected diminution in the value of the tractors. Furthermore, no evidence suggests that Paccar, or Nalley as successor-in-interest, made a business decision not to pursue adequate protection. Because neither Nalley nor Paccar acquiesced in the harm to the tractors and because the adequate protection payments would not have covered the diminution, we find no indication that Nalley's loss was caused by anything other than the imposition of the stay, Paccar's forbearance from foreclosing, and the continued use of the trucks by Debtor.

C. Evidentiary Challenges

[10][11] In addition to arguing that Nalley was not entitled to an administrative expense claim, the Trustee also contends that Nalley failed to establish the value of the tractors at the time of the stay and at the time of repossession. The Trustee alleges that Nalley presented evidence of value at the time of the stay that was not based on personal knowledge of the condition of the trucks, but rather on the "Blue Book" value of trucks in roadworthy condition. Similarly, the Trustee asserts that the proceeds from the sale to Arrow after repossession do not reflect the value of the trucks because Nalley did not prove that this sale was commercially reasonable. These challenges to the evidentiary basis of the Bankruptcy Court's ruling must be reviewed on a clearly erroneous standard. In re Club Assoc., 951 F.2d 1223 (11th Cir. 1992); In re Sublett, 895 F.2d 1381 (11th Cir. 1990). Like the District Court, we do not find that the Bankruptcy Court was clearly erroneous in accepting Nalley's evidence of the value of the collateral. Finding no clear error, we decline to disturb the factual determination of the Bankruptcy Court.

[12] The Trustee also alleges that the Bankruptcy Court erred by basing the amount of the administrative expense priority on the amount Nalley paid Paccar pursuant to its recourse obligation. Apparently, the Trustee assumes that the fact that the amount paid

by Nalley to Paccar is the same amount as the administrative expense priority granted to Nalley is proof that the Bankruptcy Court based the administrative expense grant on the amount of the recourse obligation payment. The Bankruptcy Court in fact stated that it was limiting the administrative expense priority to the amount paid on the recourse obligation in order to avoid giving Nalley a windfall. The recourse obligation was not used as the measure of damage, but merely served to limit the amount granted to Nalley as compensation for damage to the collateral. Indeed, using the figures accepted by the Bankruptcy Court, the total amount of the diminution in value claimed by Nalley as an administrative expense is approximately $406,500[3] plus various fees and expenses. Relying upon the amount of money that actually changed hands pursuant to the recourse obligation allowed the Bankruptcy Court to avoid bestowing a windfall upon Nalley by limiting the first priority administrative expense to the most tangible indication of actual out of pocket loss available. Thus, the Trustee's argument is without merit.

The District Court's judgment is affirmed.

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[3] This figure is calculated by subtracting the value of the tractors at the time of repossession, $60,000, from the value at the time of the automatic stay, $575,000, and then subtracting the amount of adequate protection provided, $108,500.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ROME DIVISION

4:91-v-82-HLM

PAUL W. BONAPFEL, TRUSTEE FOR
BANKRUPTCY ESTATE OF
CARPET CENTER LEASING CO., INC.,
Appellant

v.

NALLEY MOTOR TRUCKS,
A DIVISION OF NALLEY CHEVROLET, INC.
Appellee

[Entered January 31, 1992]

ORDER

This Case is before the Court on appeal from the Order of the Bankruptcy Court dated March 12, 1991, which allowed Nalley Motor Trucks ("Nalley") an administrative priority claim, pursuant to 11 U.S.C. § 507 (b), in the amount of $370,915.96.

I. Facts

Carpet Center Leasing Company, Inc. ("Debtor") filed its Chapter 11 petition in bankruptcy on February 25, 1987. At that time Debtor had a large fleet of trucks and trailers maintained at various locations. These trucks and trailers were security for debts

owed numerous creditors, one of which was Paccar Financial Corporation ("Paccar"). Pursuant to a retail installment contract with the debtor, Paccar received a monthly payment of $39,267.37 for the 26 trucks and trailers in which Paccar held a security interest. On March 30, 1987, Paccar filed a "Motion for Relief from the Automatic Stay," requesting permission to repossess its collateral. Before a hearing on the matter, however, Paccar and Debtor reached an agreement whereby Debtor was required to make monthly payments to Paccar in the amount of $18,661.25 as adequate protection of Paccar's security interest.

The adequate protection payments due for the months of January and February 1988, however, were not paid. Consequently on March 1, 1988, Paccar filed its second motion for relief from the automatic stay. A consent order was entered which gave Paccar the right to repossess its collateral, and which provided:

> "The within order is . . . entered without prejudice to the movant in regard to movant's right to answer an administrative claim in regard to the adequate protection payments which were not made by Debtor, and without prejudice to movant's right to assert any other claims it may have against the Estate of Debtor."

The consent order was signed by Paul Bonapfel, Appellant herein, who had become the Estate's Chapter 11 Trustee.

Following the lifting of the stay, Paccar began to repossess its collateral. It appears that most of the trucks were retrieved by Paccar by the end of April, 1988. At least one tractor, however, was received in August of 1988.

The parties to this appeal hotly contest the condition of the vehicles upon repossession. Appellee contends that the trucks were found in disrepair throughout Georgia and Alabama, with one found in a field and another found laying on its side. Only two of the 23 remaining trucks,[4] according to the Appellee, were returned in an operable condition. Appellant, on the other hand, argues that only one of the trucks was of "salvage value only" and that the rest were in operable condition.

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[4] 3 of the trucks were completely paid for by the Debtor.

Soon after repossession, Paccar sent notices relating to a public sale of the trucks and trailers. Appellant contends that these notices did not meet the applicable standards of Georgia law.[5] The last of these notices were sent on August 5, 1988. On August 19, 1988, a public sale was held in which Paccar was the only bidder and paid $89,000.00 for the repossessed trucks and trailers. Approximately two months later the trucks and trailers were sold to Arrow Truck Center Incorporated ("Arrow") for $60,000.00.

The bankruptcy case, during this same time period, was converted into a Chapter 7 proceeding. On June 24, 1988, Paul Bonapfel became the permanent Chapter 7 Trustee. On August 16, 1988, the Bankruptcy Court ordered all administrative expense claims to be filed within sixty days. On September 21, 1988, Paccar filed an administrative expense claim in the amount of $413,561.71.

On May 25, 1989, Paccar assigned its rights to Nalley Motor Trucks ("Nalley"), appellee herein, pursuant to a retail installment contract/security agreement. Under the terms of that agreement Nalley was required to pay Paccar a recourse obligation of $370,915.96. Nalley substituted itself for Paccar in these proceedings on February 12, 1990.

The Trustee filed his objection to Nalley's administrative expense claim on November 15, 1990. The matter was set for a hearing on February 26, 1991.

At the hearing, both sides were given an opportunity to produce evidence relevant to Nalley's administrative expense claim. Nalley used the blue book average value to assign a value to the trucks and trailers as of the date the bankruptcy petition was filed. This amount was shown to be $575,000.00. Nalley presented photographs of the repossessed trucks and trailers and business records containing lists of missing and defective parts for each truck to establish depreciation. Furthermore Nalley alleged that the $60,000.00 received from Arrow Truck Center was the fair market

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[5] Appellant contends that few, if any, of the public sale notices were sent within ten days of repossession. Some notices were sent which did not mention Paccar's intent to pursue a deficiency.

value of the collateral at the time of repossession. The Trustee ("Appellant") produced an expert witness who disputed Nalley's evidence of valuation.

The Bankruptcy Court accepted the Nalley's evidence and rejected that of Appellant. The Court found that the proceeds of Nalley's sale to Arrow Truck Center was strong evidence of the fair market value of the trucks and trailers at the time of repossession. The Court also found that Nalley's collateral had depreciated during the course of the bankruptcy case and the loss was attributable to the automatic stay of bankruptcy. The Bankruptcy Court concluded however, that the best indication of the amount that Nalley had been injured by the automatic stay was the amount of money Nalley had to pay in order to buy out Paccar's position pursuant to the recourse obligation.[6] Nalley was awarded $370,915.96 as an administrative expense priority under 11 U.S.C. § 507(b). This appeal has followed.

II. Arguments on Appeal

Appellant argues that the Bankruptcy Court erred in allowing Nalley an administrative expense claim. Appellant contends that Nalley lost its claim against the estate through its failure to comply with Georgia's Motor Vehicle Sales Finance Act and Commercial Code. Second, Appellant argues that the Bankruptcy Court erred in valuing Nalley's administrative expense claim at $370,915.96. Appellant contends that the court should not have adopted Nalley's evidence of valuation and that the Court erred in concluding that Nalley's loss was attributable to the stay of bankruptcy.

Appellant's first argument is based on two premises: (1) that a claim under 11 U.S.C. § 507(b) is limited to the amount of the total debt; and, (2) that such claims are, in substance, deficiency claims. Appellant argues that Nalley's alleged noncompliance with

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[6] The evidence produced by Nalley showed a much greater diminishment in value. Given that the value of the trucks and trailers on the date of petition was $575,000, and at the conclusion of the bankruptcy case was only $60,000, Nalley's proof indicated a loss of some $415,000.

Georgia's Motor Vehicle Sales Finance Act and Commercial Code barred any attempt by Nalley to collect a deficiency. Therefore, Nalley's sole recourse became the repossessed collateral, and Nalley's claim against the debtor's estate was extinguished. Because Nalley has no claim against the Debtor's estate, it can assert no claim for an administrative expense pursuant to 11 U.S.C. § 507(b).

Appellant's second argument attacks the factual premises and legal conclusions of the Bankruptcy Court's decision. Appellant argues that the Bankruptcy Court's valuation of the collateral following repossession was erroneous and that the Bankruptcy Court should not have concluded that the automatic stay caused Nalley's loss.

Nalley defends the decision of the Bankruptcy Court. Nalley contends that its administrative expense claim is not a deficiency claim and is not subject to the MVSFA or Georgia's Commercial Code. Nalley also defends the findings of the Bankruptcy Court which support its award of $370,915.96.

III. Whether Administrative Expense Claims pursuant to 11 U.S.C. § 507(b) are Barred by Failure to Comply with State Foreclosure Law.

The central issue for resolution is whether failure to comply with state foreclosure laws bars a claim for an administrative expense pursuant to 11 U.S.C. § 507(b). This is, apparently, a case of first impression.

As to the relationship between state law and the bankruptcy rules, however, the leading case appears to be *Vanston Bondholders Protective Committee v. Green*, 329 U.S. 156 (1946).[7] In *Vanston*, the Supreme Court held that federal caselaw under the Bankruptcy Act, and developed in federal equity receiverships, barred a claim which was otherwise valid under state law. *Id.*, at 165; *See also*, *In re Yanks*, 49 B.R. 58 (Bankr. S.D.Fla. 1985). The Court found

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[7] Although *Vanston* was decided under the forerunner of the present Bankruptcy Code, the Bankruptcy Act, its holding is still followed today. *See*, *In Re A.H. Robins Co., Inc.*, 89 B.R. 555 (E.D. Va. 1988).

that state law determines which creditor's claims are valid against the debtor at the time of bankruptcy *only in the absence of overruling federal law*. "In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state in which it sits. . . .[B]ankruptcy courts must administer and enforce the Bankruptcy Act as interpreted by this Court in accordance with authority granted by Congress to determine how and what claims shall be allowed under equitable principles." *Vanston*, 329 U.S., at 162-63.

Several courts have used the authority set forth in *Vanston* to decide whether, based on equitable principles rather than state law, claims in bankruptcy should be allowed. *In re Dodge*, 101 B.R. 800 (Bankr. S.D.Fla. 1989); *Matter of Ovetsky*, 100 B.R. 115 (Bankr. N.D.Ga. 1989); *In re Central Foundry Co.*, 62 B.R. 52 (Bankr. N.D.Ala. 1985); *In re Yanks*, 49 B.R. 56 (Bankr. S.D.Fla. 1985). In *Matter of Ovetsky*, supra, for example, the Court was faced with the question of whether the five year Missouri statute of limitations or the two year Georgia statute of limitations determined the timeliness of a claim against a debtor's estate. The Court found that under *Vanston*, supra, the Court was not bound to apply Georgia conflict law and went on to determine the question based on its examination of the "equities of the situation." *Ovetsky*, 100 B.R., at 117.[8]

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[8] In *Matter of Winslow*, 39 B.R. 869 (Bankr. N.D.Ga. 1984), cited by Appellant, the Court refused to allow a creditor to assert a claim for a deficiency following its repossession of an automobile from a debtor who had filed for protection under Chapter 13 of the Bankruptcy Code on the grounds that the creditor had failed to comply with state foreclosure law. The court reasoned that when an order lifting the automatic stay of bankruptcy is entered, the parties are returned to the legal relationships which existed before the stay became operative. While the Court in *Matter of Winslow* did not apply the principles enunciated in *Vanston* to achieve its result, the court's conclusion was certainly not incompatible with *Vanston*. *Vanston* stands for the proposition that federal law and equitable principles, rather than state law, controls the determination of whether a claim in bankruptcy should be allowed. It does not hold that state law is irrelevant.

Applying the rule set forth in *Vanston* to the case at bar, compliance with state law, or lack thereof, is but one equitable consideration to be weighed in the balance with others to determine whether Nalley's claim for an administrative expense should be allowed.

Appellant argues that *Vanston* does not control the analysis in this case since *Vanston* deals only with the allowance of claims, rather than the threshold question of whether a claim exists. Appellant contends that because Nalley lost its claim against the estate, is *Vanston* irrelevant. There is no claim to allow.

Appellant's principle argument is based on Georgia's Motor Vehicle Sales Finance Act ("MVSFA"), O.C.G.A. 10-1-30 *et. seq.*, which provides in part:

> "When any motor vehicle has been repossessed after default . . . the seller or holder shall not be entitled to recover a deficiency against the buyer unless within ten days after the repossession he forwards by registered or certified mail to the address of the buyer shown on the contract or later designated by the buyer a notice of the seller's or holder's intention to pursue a deficiency claim against the buyer. The notice shall also advise the buyer of his right of redemption, as well as his right to demand a public sale of the repossessed vehicle . . . This code section is cumulative of part 5 of Article 9 of Title 11 and provides cumulative additional rights and remedies which must be fulfilled before any deficiency claim will lie against a buyer, and nothing herein shall be deemed to repeal aid part."

O.C.G.A. 10-1-36. Compliance with the MVSFA is an absolute prerequisite to recovery of a deficiency claim. *See, Bryant*

International, Inc. v. Crane, 188 Ga. App. 736 (1988); *Doughty v. Associates Commercial Corp.*, 152 Ga. App. 575 (1979).

Appellant contends that once the automatic stay was lifted, and Nalley allowed to repossess its collateral, Nalley was required to act in compliance with the MVSFA, as well as Georgia's Commercial Code.[9] Appellant argues that Nalley failed to send notice of its intent to collect a deficiency within ten days as required by MVSFA. The result of this failure, according to Appellant, was that Nalley's claim against the estate was extinguished.

Appellant's argument on the basis of Georgia's Commercial Code is similar. Appellant contends that Nalley's disposition of its collateral following foreclosure did not comply with the provisions of Georgia's Commercial Code. *See*, O.C.G.A. 11-9-504(3). Failure to comply with the dictates of the Georgia Commercial Code in a foreclosure sale results in a rebuttable presumption that the value of the collateral sold is equal to the indebtedness owed and can, should the creditor fail to show the reasonableness of its actions, result in the loss of the creditor's right to seek a deficiency. *Contestable v. Business Development Corporation of Georgia*, 259 Ga. 783 (1990). Appellant argues that Nalley's sale of the repossessed trucks and trailers cannot be justified as commercially reasonable and, therefore, the debt owed Nalley by the debtor's estate is deemed equal to the value of the repossessed collateral. Consequently, Nalley is left without a claim against the debtor's estate.

Appellant contends that any claim Nalley may have had for an administrative expense was also barred by its failure to comply with Georgia's MVSFA and Commercial Code. Since administrative expense claims are limited to the total amount of debt owed, when Nalley's claim against the estate was extinguished, the limit of Nalley's administrative expense claim became zero. Appellant also argues that attaching the label "administrative

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[9] Appellant points out that the order of the Bankruptcy Court, which lifted the automatic stay, specifically provided that Nalley could foreclose on its collateral in accordance with the laws of Georgia.

expense" to Nalley's claim does not change the fact that it is, in substance, a deficiency claim.

In the view of this Court, however, Appellant's argument is based upon flawed conceptions of both Georgia's law of foreclosure and administrative claims in bankruptcy. This Court finds that the alleged inadequacies in Nalley's post repossession conduct does not negate the existence of Nalley's claim against the debtor's estate. Moreover, this Court is not persuaded that an administrative expense claim can be considered a deficiency claim.

Appellant has argued that under Georgia's MVSFA, and Commercial Code, Nalley lost any claim that it had against the estate. This is not accurate. Although noncompliance with the terms of the MVSFA bars the prosecution by a creditor of a deficiency claim, it does not affect the existence of such claim. Georgia's MVSFA speaks only of a creditor's entitlement to "recover a deficiency against the buyer." O.C.G.A. 10-1-36. Compliance with the MVSFA is simply a condition precedent to recovery of a deficiency claim. *Doughty v. Associates Commercial Corporation*, 152 Ga.App. 575 (1979). Similarly, any infirmities in the post repossession conduct of creditors under Georgia's Commercial Code does not absolve the underlying debt. *See*, O.C.G.A. 11-9-504(3). In the case of the Commercial Code, a creditor's failure to comply with its terms results in the creation of a rebuttable presumption that the value of the collateral is equal to the debt. A creditor must prove the reasonableness of his actions. He does not, however, lose his claim.

Nor does this Court accept Appellant's argument that the administrative expense claim brought by Nalley in this case is, in essence, a deficiency claim. An administrative expense claim, pursuant to 11 U.S.C. § 507(b), is a creature of the Bankruptcy Code and its existence can be attributed directly to the policy decisions made by Congress.

Under the Bankruptcy Code, a debtor who files for protection is given a statutory refuge, the Automatic Stay. *See*, 11 U.S.C. § 362(a). The automatic stay prevents creditors from undertaking any acts to seize assets of the bankrupt estate. The stay is designed to give debtors a "breathing spell" and prevent a "chaotic and uncontrolled scramble for the debtor's assets in a

variety of uncoordinated proceedings in different courts." *Fidelity Mortgage Investors v. Camelia Builders, Inc.*, 550 F.2d 47, 55 (2d Cir. 1976).

Under the automatic stay, the debtor continues to use the protected assets as he tries to restructure his finances. The danger for the creditor in this situation is that the assets it relies upon for security will depreciate. The drafters of the Bankruptcy Code sought to mitigate this danger through 11 U.S.C. § 362(d) which allows a secured creditor to seek "adequate protection" of its interest in certain collateral. *In re Cheatham*, 91 B.R. 382 (E.D.N.Y. 1988). Adequate protection generally takes the form of a periodic cash payment or other security which is intended to keep constant the value of a secured creditor's interest in the debtor's estate. *Id.*, at 387.

It is, of course, difficult to predict an asset's real depreciation. The Bankruptcy Code's solution for this problem is to allow creditors an administrative expense claim pursuant to 11 U.S.C. § U.S.C. 507(b). Section 507(b) provides as follows:

> "If the trustee, under section 362, 363 or 364 of this title, provides adequate protection of the interest of a holder of a claim secured by a lien on property of a debtor and if, notwithstanding such protection, such creditor has a claim allowable under subsection (a)(1) of this section arising from the stay of action against the property under section 362 of this title, from the use, sale, or lease of such property under section 363 of this title or from the granting of a lien under section 364(d) of this title, then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection."

Section 507(b) covers situations in which adequate protection has been given to a secured creditor and later proves to be inadequate.

The creditor in such a situation becomes eligible for an admnistrative expense claim to the extent that the proffered adequate protection was insufficient. *In re James B. Downing & Co.*, 94 B.R. 515 (Bankr. N.D.Ill. 1988); *In re Mutschler*, 45 B.R. 494 (Bankr. D.N.D. 1984).

The administrative expense claim is thus part of a carefully balanced system of benefits and burdens created by Congress. The claim arises from the unique circumstances of a bankruptcy case and is legally distinct from any nonbankruptcy theory. It is not a deficiency claim.

Moreover, in the instant case, both sides have recognized Nalley's right to assert an administrative expense claim. The consent order which lifted the automatic stay and allowed repossession specifically addressed Nalley's right to assert an administrative claim at least for the adequate protection payments which had been missed. This Court cannot, therefore, accept Appellant's argument that Nalley has no claim against the Debtor's Estate.

Having found that Nalley does possess a claim against the debtor's estate, the next question is whether that claim should be allowed against the debtor's estate.

Under *Vanston*, supra, a bankruptcy court must rely on federal law and equitable principles in deciding whether to allow claims in bankruptcy. Federal law clearly authorizes an administrative expense claim in situations such as the one at bar. Two conditions must be met before a court is authorized to award an administrative expense claim: (1) the secured creditor must have been provided adequate protection of its security interest in property of the debtor's estate; and (2) the adequate protection approved by the court must later be proven to be inadequate. *In re James B. Downing & Co.*, 94 B.R. 515 (Bankr. N.D.Ill. 1988); *In re Mutschler*, 45 B.R. 494 (Bankr. D.N.D. 1984).

> "If the adequate protection given by the court proves to be inadequate, that is, the secured creditor winds up being injured from the continuation of the stay, use of the property, or funding of the estate in the sense that its

> unsecured deficiency claim against the estate is increased, the creditor is entitled to a superpriority for the increase in the deficiency."

In re James B. Downing & Co., *supra*, 94 B.R., at 521, *quoting*, Ginsberg, *Bankruptcy* § 10,705 (1986).

Of course, proof of legal entitlement is not the end of the inquiry in determining whether to allow a claim in bankruptcy. Courts are entitled under the Bankruptcy Code to disallow valid claims where recognition of such claims would undermine the fair administration of a debtor's estate. *In re A. H. Robbins Co.*, 89 B.R. 555 (E.D. Va. 1988). "It is manifest that the touchstone of each decision on allowance of an interest in bankruptcy . . . has been a balance of equities between creditor and creditor or between creditors and the debtor." *Vanston*, 329 U.S., at 241.

Appellant has argued forcefully that under equitable principles Nalley's claim should not be allowed. First, assuming Nalley would not be able to assert a claim against the estate for a deficiency, it is inequitable to allow Nalley a recovery tantamount to a deficiency as an administrative expense. Second, allowance of Nalley's claim, Appellant contends, would inequitably enrich Nalley at the expense of other creditors since the size of Nalley's claim is directly related to Nalley's own conduct.

As to the first argument, this Court is aware of the similarity between the recovery Nalley would receive as an administrative expense and what it would receive as a deficiency. Nalley stands in the shoes of a creditor who was fully secured at the time the bankruptcy petition was filed. Consequently, calculating an administrative expense claim in terms of the amount that Nalley's collateral depreciated during the pendency of the bankruptcy case results in a figure very similar to that Nalley would be entitled to as a deficiency.[10] Asserting a claim for an administrative expense rather than a claim for a deficiency, however, gives Nalley two

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[10] A deficiency claim would be calculated by referring to the remaining sums outstanding on the contracts and deducting therefrom the proceeds obtained at resale and the adequate protection payments made.

ostensible advantages. First, Nalley's claim is not potentially barred for failure to give notice and hold a commercially reasonable sale, as those terms are defined under state law.[11] Second, an administrative expense claim asserted under 11 U.S.C. § 507(b) is entitled to priority over the claims of other creditors.

These ostensible advantages, upon closer examination, do not persuade this Court should disallow Nalley's claim. The principal purpose of the statutory notice and sale provisions of Georgia's MVSFA and Commercial Code are to ensure that a creditor receives a fair market value for repossessed goods before asserting a deficiency claim against the debtor. *See, Barnett v. Trussell Ford*, 129 Ga. App. 176 (1973); *Brown v. CIT Corp.*, 150 Ga. App. 361 (1979). This purpose is also served where a claim is asserted under § 507(b). An administrative claim under 11 U.S.C. § 507(b) is limited to the actual loss incurred by a secured creditor due to a decrease in its interest in the property during the pendency of the bankruptcy, and attributable to the stay of bankruptcy. *In re Colter, Inc.*, 53 B.R. 958 (Bankr. D.Colo. 1985).

> "Creditors may acquiesce in some harm to collateral for business or other reasons notwithstanding the stay. In these situations and others which may arise, any impairment in value may not be attributable to the stay. Hence, not every decline in value must be recompense, only those which, but for the stay, could be and probably would be mitigated."

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[11] Whatever the force of *Matter of Winslow*, supra, under *Vanston*, supra, *Winslow* at least stands as an example of the disallowance of a deficiency claim in bankruptcy where a creditor failed to comply with state foreclosure laws. Equitable considerations are unlikely to change this result. The case was even cited by the Eleventh Circuit for the proposition that when the stay of bankruptcy is lifted the parties relationship is governed by whatever nonbankruptcy law governed that relationship before the bankruptcy. *See, Kahihikolo v. General Finance Corporation*, 807 F.2d 1540 (11th Cir. 1987).

In re Falwell Excavating Co., Inc., 47 B.R. 217, 220 (Bankr. W.D.Va. 1985), *quoting In re Callister*, 15 B.R. 521, 530 (Bankr. D.Utah 1981); *In re Alyucan Interstate Corp.*, 12 B.R. 803 (Bankr. D.Utah 1981). Consequently, if a creditor fails to dispose of his property in a commercially reasonable manner following foreclosure, his loss cannot not be attributed to the stay of bankruptcy. Moreover, the burden is on the creditor claiming an administrative expense to prove his loss was attributable to the stay. *In re Becker*, 51 B.R. 975 (Bankr. D.Minn. 1985); *In re B & W Tractor Co., Inc.*, 38 B.R. 613 (Bankr. E.D.N.C. 1984).

The fact a secured creditor gains priority over other creditors by pursuing an administrative expense claim instead of a deficiency judgment is also not grounds for disallowance of the claim in equity. As the Bankruptcy Court in this case stated, the goal of 11 U.S.C. 507(b) is to protect the reasonable business expectations of a secured creditor. The superpriority afforded administrative expense claims under § 507(b) is the "statutory fail-safe system" by which secured creditors, who are granted adequate protection, receive just that. *See, Callister*, 15 B.R., at 528. This priority represents the policy decision of Congress.

Appellant's remaining arguments all deal with Nalley's alleged conduct in protecting and disposing of its collateral. Nalley is alleged to have sat on its rights throughout the pendency of the bankruptcy case and to have chilled the final sale price of the trucks to Arrow. Nalley, on the other hand, argues that its predecessor in interest, rather than sitting on its rights, negotiated in good faith during the pendency of the bankruptcy case with an eye toward rehabilitating the debtor and preserving the debtor's business as a going concern. After foreclosure, Nalley contends that it disposed of the trucks as best it could, given the limited market for salvage value trucks.

The material facts which weight on the issue of whether Nalley's conduct was so egregious that its administrative expense claim should be disallowed in equity were determined by the Bankruptcy Court. The Bankruptcy Court was not persuaded that Nalley chilled the bidding during its sale of the trucks and trailers, or that the decrease in value of the collateral was caused by anything other than the stay of bankruptcy. These factual findings have

support in the record and this Court cannot say that they are clearly erroneous. Consequently, this Court finds no ground for disallowance of Nalley's claim in equity.

IV. Whether the Bankruptcy Court's Decision to Award $370,915.96 to Nalley pursuant to 11 U.S.C. § 507(b) was justified by the record.

Appellant has objected to the findings of the Bankruptcy Court which provide the basis of that Court's award of an administrative expense claim in the amount of $370,915.96. Specifically Appellant objects to the Bankruptcy Court's findings that: (1) the fair market value of the repossessed trucks and trailers at the time of repossession was $60,000.00; and, (2) that Nalley's loss was attributable to the automatic stay.

The Bankruptcy Code does not prescribe any particular method of valuation leaving such matters to be determined by judges on a case by case basis. *Matter of Clark Pipe & Supply Company, Inc.*, 893 F.2d 693 (5th Cir. 1990). "Valuation is a mixed question of law and fact, the factual premises being subject to review on a "clearly erroneous" standard, and the legal conclusions being subject to *de novo* review." *Id.*, at 698; *In re Ebbler Furniture and Appliances, Inc.*, 804 F.2d 87 (7th Cir. 1986).

Appellant asserts that the conclusion of the Bankruptcy Court as to valuation should be overturned since the Court considered the resale price of the collateral to be its fair market value. Appellant argues that there was no evidence from which the Court could conclude that Nalley's sale of the repossessed trucks to Arrow was commercially reasonable, and that Nalley failed to present conclusive evidence of the collateral's value at the time of repossession. The Bankruptcy Court, in Appellant's opinion, relied on the faulty premise that the repossessed collateral was of "salvage value only," and failed to take into consideration the fact that the sale of the trucks took place six months after repossession. Consequently, Appellant contends, the legal conclusion that the sale of the collateral equals its fair market should be overturned.

This Court does not agree. Nalley presented photographs of the trucks taken at the time the trucks were repossessed, as well as

lists of all parts which the trucks were missing. Nalley also produced an expert who testified as to the trucks value. This evidence was used by the Bankruptcy Court to determine that the collateral had depreciated during the pendency of the bankruptcy case through the debtor's use. Nalley also presented evidence that the sale to Arrow was an arms length transaction which took place in a limited market for salvage value trucks.

In response to Nalley's evidence, Appellant produced an expert who had not inspected any of the trucks and trailers involved. Appellant's expert testimony as to the value of the trucks was based only on his examination of the photographs supplied by Nalley.

The crux of this valuation dispute is whether the trucks were of salvage value only, as Nalley's expert testified, or were reasonably operable, as the Appellant's expert testified. This dispute accounts for the widely divergent views of the evidence adduced before the Bankruptcy Court. The Bankruptcy Court found for Nalley on this question and the Court's subsequent conclusions about the sale to Arrow and the ultimate valuation of the collateral followed from this finding. This determination is a purely factual matter which can be overturned only if clearly erroneous. This Court, however, does not find that the Bankruptcy Court's conclusion was clearly erroneous.

Likewise, this Court does not find error in the Bankruptcy Court's valuation of the collateral. While the sale price of collateral is not, in and of itself, evidence of fair market value, *In re Lenz*, 110 B.R. 523 (D.Colo. 1990), such evidence can be used to establish fair market value. In the instant case the Bankruptcy Court also had evidence of the recourse obligation between Nalley and Paccar. The Bankruptcy Court found that this recourse obligation was an arms length transaction which accurately reflected the secured creditor's loss attributable to the debtor's use of the collateral during the bankruptcy case. In sum, this Court's own review of the evidence does not lead to the conclusion that the Bankruptcy Court erred in its valuation of the collateral.

Appellant's last enumeration of error is that the Bankruptcy Court erred in its determination that Nalley's loss was attributable to the stay of bankruptcy and not to Nalley's own behavior. This finding is reviewable only under the clearly erroneous standard. *In*

re Sublett, 895 F.2d 1381 (11th Cir. 1990); *In re Thomas*, 883 F.2d 991 (11th Cir. 1989). The Bankruptcy Court found that Nalley's injury attributable to the stay of bankruptcy exceeded the amount of adequate protection payments at least by the amount of the recourse obligation between Nalley and Paccar. There is support for this finding in the record, and this Court's review of all the evidence does not indicate that the Bankruptcy Court's conclusion was erroneous.

V. Conclusion

Accordingly, based on the above, the decision of the Bankruptcy Court is AFFIRMED.

IT IS SO ORDERED, this 31st day of January, 1991. [sic]

ENTERED FOR THE COURT:

S\HAROLD L. MURPHY
UNITED STATES DISTRICT JUDGE

APPENDIX C

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ROME DIVISION

R87-00196-HR

NALLEY MOTOR TRUCKS, A DIVISION OF
NALLEY CHEVROLET, INC.
Movant

v.

PAUL W. BONAPFEL, AS TRUSTEE
FOR THE ESTATE OF
CARPET CENTER LEASING COMPANY, INC.
Respondent

[Entered March 12, 1991]

ORDER AWARDING MOVANT NALLEY MOTOR TRUCKS A $370,915.96 SUPERPRIORITY EXPENSE PURSUANT TO BANKRUPTCY CODE SECTION 507(b)

WHEREAS, Nalley Motor Trucks, a division of Nalley Chevrolet, Inc. ("NALLEY"), Movant herein, is the duly recognized successor-in-interest to Paccar Financial Corporation ("PACCAR"), a creditor and party in interest in the above-styled and numbered Chapter 7 bankruptcy case;

WHEREAS, various over-the-road tractors ("tractors") were used by the Debtor, and certain of them were subject to a security interest retained by PACCAR;

WHEREAS, an Adequate Protection Order was entered in this case pertaining to PACCAR's interest in the referenced tractors as a secured creditor, in consideration for Debtor's continued use of said collateral;

WHEREAS, the automatic stay was subsequently lifted to allow PACCAR to repossess and dispose of said tractors;

WHEREAS, PACCAR timely filed a Motion for Allowance of and Proof of Administrative Expense and Claim, and PACCAR also filed a Proof of Claim;

WHEREAS, the Chapter 7 Trustee, Paul W. Bonapfel, by and through his attorneys, filed a Response Objecting to Motion for Allowance of and Proof of Administrative Expense and Claim requested by Movant;

WHEREAS, NALLEY filed a Reply to Trustee's Response Objecting to Motion for Allowance of and Proof of Administrative Expense and Claim Requested by Movant;

WHEREAS, the foregoing matters came before the Court for a hearing on February 26, 1991; and

WHEREAS, the Court considered the aforementioned pleadings, having also considered the arguments presented by counsel for NALLEY and for the Trustee at the hearing, including the testimony given by expert witnesses on behalf of both parties, as well as exhibits submitted by NALLEY that were admitted into evidence.

NOW, THEREFORE, IT IS HEREBY ORDERED THAT NALLEY shall be allowed a superpriority claim against the estate in the amount of $370,915.96 pursuant to Bankruptcy Code Section 507(b). Said amount reflects the diminution in value of the over-the-road tractors which were used by the Debtor and which were subject to PACCAR's security interest, and it reflects the actual damage consequently suffered by NALLEY as the duly recognized successor-in-interest to PACCAR.

It is further ORDERED that this award of $370,915.96 to NALLEY as a superpriority claim against the estate pursuant to

Bankruptcy Code Section 507(b) shall have priority over every other claim allowable pursuant to Bankruptcy Code Section 507(a)(1).

It is additionally ORDERED that NALLEY is entitled to assert a general unsecured claim for additional damages, subject to objection by the Trustee, pursuant to PACCAR's contractual rights with Debtor which were assigned to NALLEY, and for which NALLEY may not be sufficiently compensated by the foregoing superpriority award of $370,915.96, and NALLEY shall take whatever action is required to assert and delineate such a claim.

SO ORDERED this 12 day of March, 1991 at Rome, Georgia.

ENTERED FOR THE COURT:

S\HUGH ROBINSON
UNITED STATES BANKRUPTCY JUDGE

PREPARED AND SUBMITTED BY:

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Nalley Motor Trucks, a
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APPENDIX D

IN THE UNITED STATES COURT OF APPEALS
ELEVENTH CIRCUIT

No. 92-8223

PAUL W. BONAPFEL, AS TRUSTEE
FOR THE ESTATE OF
CARPET CENTER LEASING COMPANY, INC.
Plaintiff-Appellant

v.

NALLEY MOTOR TRUCKS, A DIVISION OF
NALLEY CHEVROLET, PACCAR FINANCIAL CORP.
Defendants-Appellees

Appeal from the United States District Court
for the Northern District of Georgia

ON PETITION FOR REHEARING AND
SUGGESTION OF REHEARING EN BANC

[Entered September 30, 1993]

Before KRAVITCH and ANDERSON, Circuit Judges, and HILL, Senior Circuit Judge.

PER CURIAM:

Upon consideration of the appellant's Petition for Rehearing, the panel has concluded that the original opinion at 991 F.2d 682 (11th Cir.1993) be amended by adding the following paragraphs immediately following the final paragraph of Part II.A:

The Trustee's reliance on s 361(3) is misplaced. Section 361(3) states that adequate protection required under section 362, 363, or 364 may be provided by "granting such other relief, *other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense*, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property." 11 U.S.C. § 361(3) (emphasis added). Although this language, at first blush, seems to contradict the allowance of such an administrative expense claim as in § 507(b), the legislative history of § 361(3) clarifies the issue.

Section 361(3) prohibits only the granting of an administrative expense claim as adequate protection *as an initial matter*. In drafting this provision, Congress was concerned about undersecured creditors being lured into forgoing the right to foreclose on collateral by the illusory promise of an administrative expense claim, when the estate's assets would later prove to be insufficient to make such payments. 124 Cong.Rec. 32,395 (1978) ("In every case there is the uncertainty that the estate will have sufficient property to pay administrative expenses in full."). Hence, the goal of § 361(3) is to protect creditors, not debtors, and its prohibition applies only to the initial form of adequate protection allowed. Despite this ex ante prohibition on the use of an administrative expense claim, it is specifically allowed as a *remedy* for the later failure of the adequate protection granted. The legislative history reinforces this construction: "To the extent the protection proves to be inadequate *after the fact*, the creditor is entitled to a first priority administrative expense under section 503(b)." *Id.* (emphasis added).

Section 507(b) thus implies that an administrative expense claim under § 503(b) will be allowed where adequate protection payments prove insufficient to compensate a secured creditor for the

diminution in the value of its collateral. "It is an attempt to codify 'a statutory fail-safe system in recognition of the ultimate reality that protection previously determined the "indubitable equivalent"...may later prove inadequate.' " *In re Becker*, 51 B.R. 975, 979 (Bankr. D.Minn. 1985) (quoting *In re Marine Optical, Inc.*, 10 B.R. 893, 894 (Bankr.D.Mass.1981)).

This construction of the Code makes clear that Nalley's claim for administrative expenses arose, not from any deficiency claim based on the underlying pre-petition obligation, but entirely under § 503(b) as an post-petition "actual, necessary cost[ ] and expense[ ] of preserving the estate." 11 U.S.C. § 503(b). Consequently, the bankruptcy court and the district court correctly held that compliance with state law is irrelevant to the allowance of a claim for administrative expenses under § 507(b).

Except as above amended, the original opinion shall remain in full force and effect.

The Petition for Rehearing is DENIED and no member of this panel nor other Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Eleventh Circuit Rule 35-5), the Suggestion of Rehearing En Banc is DENIED.

APPENDIX E

1. 11 U.S.C. § 361 provides:

> When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by--
> (1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;
> (2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or
> (3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property

2. 11 U.S.C. § 362 provides in pertinent part:

> (a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title. . ., operates as a stay, applicable to all entities, of--
> (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;

(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

(4) any act to create, perfect, or enforce any lien against property of the estate;

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;

(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and

(8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

* * *

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay--

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property under subsection (a) of this section if--

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization.

(e) Thirty days after a request under subsection (d) of this section for relief from the stay of any act against property of the estate under subsection (a) of this section, such stay is terminated with respect to the party in interest making such request, unless the court, after notice and a hearing, orders such stay continued in effect pending the conclusion of, or as a result of, a final hearing and determination under subsection (d) of this section. A hearing under this subsection may be a preliminary hearing, or may be consolidated with the final hearing under subsection (d) of this section. The court shall order such stay continued in effect pending the conclusion of the final hearing under subsection (d) of this section if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the conclusion of such final hearing. If the hearing under this subsection is a preliminary hearing, then such final hearing shall be commenced not later than thirty days after the conclusion of such preliminary hearing.

(f) Upon request of a party in interest, the court, with or without a hearing, shall grant such relief from the stay provided under subsection (a) of this section as is necessary to prevent irreparable damage to the interest of an entity in property, if such interest will suffer such damage before there is an opportunity for notice and a hearing under subsection (d) or (e) of this section.

(g) In any hearing under subsection (d) or (e) of this section concerning relief from the stay of any act under subsection (a) of this section--

(1) the party requesting such relief has the burden of proof on the issue of the debtor's equity in property; and

(2) the party opposing such relief has the burden of proof on all other issues.

3. 11 U.S.C. § 502(b)(1) provides in pertinent part:

> (b) . . . the court, after notice and a hearing, shall determine the amount of [the] claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that--
>
> > (1) such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured;

4. 11 U.S.C. § 503(b) provides in pertinent part:

> (b) After notice and a hearing, there shall be allowed, administrative expenses, other than claims allowed under section 502(f) of this title, including--
>
> > (1)(A) the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case;

5. 11 U.S.C. § 507(b) provides in pertinent part:

> (b) If the trustee, under section 362, 363, or 364 of this title, provides adequate protection of the interest of a holder of a claim secured by a lien on property of the debtor and if, notwithstanding such protection, such creditor has a claim allowable under subsection (a)(1) of this section arising from the stay of action against such property under section 362 of this title, from the use, sale, or lease of such property under section 363 of this title, or from the granting of a lien under section 364(d) of this title, then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection.

6. 11 U.S.C. § 558 provides:

> The estate shall have the benefit of any defense available to the debtor as against any entity other than the estate, including statutes of limitation, statutes of frauds, usury, and other personal defenses. A waiver of any such defense by the debtor after the commencement of the case does not bind the estate.

7. Official Code of Georgia Annotated § 10-1-36 provides:

> When any motor vehicle has been repossessed after default in accordance with Part 5 of Article 9 of Title 11, the seller or holder shall not be entitled to recover a deficiency against the buyer unless within ten days after the repossession he forwards by registered or certified mail to the address of the buyer shown on the contract or later designated by the buyer a notice of the seller's or holder's intention to pursue a deficiency claim against the buyer. The notice shall also advise the buyer of his rights of redemption, as well as his right to demand a public sale of the repossessed vehicle. In the event the buyer exercises his right to demand a public sale of the goods, he shall in writing so advise the seller or holder of his election by registered or certified mail addressed to the seller or holder at the address from which the seller's or holder's notice emanated within ten days after the posting of the original seller's or holder's notice.
>
> In the event of election of such public sale by the buyer, the seller or holder shall dispose of said repossessed motor vehicle at a public sale as provided by law, to be held in the state and county where the original sale took place, or the state and county where the motor vehicle was repossessed, or the state and county of the buyer's residence, at the seller's election.
>
> This Code section is cumulative of Part 5 of Article 9 of Title 11 and provides cumulative additional rights and

remedies which must be fulfilled before any deficiency claim will lie against buyer, and nothing herein shall be deemed to repeal said part. (Ga. L. 1967, p. 674, § 7.)

8. Official Code of Georgia Annotated § 11-9-504(3) provides in pertinent part:

(3) Disposition of the collateral may be by public or private proceedings and may be made by way of one or more contracts. Sale or other disposition may be as a unit or in parcels and at any time and place and on any terms but every aspect of the disposition including the method, manner, time, place, and terms must be commercially reasonable. Unless collateral is perishable or threatens to decline speedily in value or is of a type customarily sold on a recognized market, reasonable notification of the time and place of any public sale or reasonable notification of the time after which any private sale or other intended disposition is to be made shall be sent by the secured party to the debtor, if he has not signed after default a statement renouncing or modifying his right to notification of sale. In the case of consumer goods no other notification need be sent. In other cases notification shall be sent to any other secured party from whom the secured party has received (before sending his notification to the debtor or before the debtor's renunciation of his rights) written notice of a claim of an interest in the collateral. The secured party may buy at any public sale and if the collateral is of a type customarily sold in a recognized market or is of a type which is the subject of a widely distributed standard price quotations he may buy at private sale.

Supreme Court, U.S.
FILED
JAN 28 1994
OFFICE OF THE CLERK

No. 93-1075

In The

Supreme Court of the United States

October Term, 1993

PAUL W. BONAPFEL, Chapter 7 Trustee
for the Bankruptcy Estate of
CARPET CENTER LEASING CO., INC.,

Petitioner,

v.

NALLEY MOTOR TRUCKS, a Division of
NALLEY CHEVROLET, INC.,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW

1. Whether Petitioner has established a sufficient basis pursuant to Sup.Ct.R. 10 to justify a grant of certiorari by the Supreme Court?

2. Whether the courts below properly ruled upon the issues adjudicated between Petitioner and Respondent, thereby justifying the award of $370,915.96 to Respondent pursuant to 11 U.S.C. § 507(b)?

PARTIES TO THE PROCEEDING IN THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

Pursuant to Sup.Ct.R. 29.1, Respondent is Nalley Motor Trucks, a division of Nalley Chevrolet, Inc., the latter being a corporation that has not issued any shares of common stock to the public. There are no other parent companies or subsidiaries of Nalley Motor Trucks or Nalley Chevrolet, Inc.

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Nalley Motor Trucks, a division of Nalley Chevrolet, Inc., respectfully urges that this Court deny the petition for writ of certiorari seeking review of the Eleventh Circuit's opinion in this case. That opinion is reported at 991 F.2d 682 (11th Cir. 1993) and at 4 F.3d 940 (11th Cir. 1993).[1]

OPINIONS BELOW

After a full day trial conducted on February 26, 1991, the United States Bankruptcy Court for the Northern District of Georgia, Rome Division, entered an order on March 12, 1991, awarding Respondent an administrative priority claim in the amount of $370,915.96 pursuant to 11 U.S.C. § 507(b). The award was based upon the diminution in value to Respondent's collateral[2] that occurred because of Debtor's use and benefit of Respondent's collateral during the pendency of the Chapter 11 bankruptcy proceeding and because of the imposition of the automatic stay in bankruptcy. The Bankruptcy Court held that the existence of Respondent's claim as well as the measurement of the diminution in value of Respondent's collateral pursuant to 11 U.S.C. § 507(b) were to be determined according to federal equitable principles, *not* the Georgia Motor Vehicle Sales Finance Act ("MVSFA"), O.C.G.A. § 10-1-36, or Georgia's Uniform Commercial Code, O.C.G.A. § 11-9-504(3). The award was also based upon Respondent's extensive photographic records[3] and Used Vehicle Appraisal Reports that were admitted into evidence by the Bankruptcy Court, as well as Respondent's expert witness testimony. The trial transcript, exclusive of the referenced photographic records and Used Vehicle Appraisal Reports, exceeds two

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[1] In response to the Petition for Rehearing and Suggestion of Rehearing En Banc filed by Petitioner, the Eleventh Circuit's second reported opinion expanded the scope of the former decision.

[2] Originally consisting of twenty-six (26) over-the-road tractors.

[3] Attached to the trial transcript is Respondent's Exhibit No. 1, which collectively refers to thirty-seven (37) photographs that were taken by Respondent of the tractors within a day or two of their return to Respondent. *Counsel for Petitioner stipulated to their admission into evidence without objection.*

hundred pages. Petitioner failed to proffer any photographic evidence or Used Vehicle Appraisal Reports of his own, and instead merely relied upon the evidence introduced by Respondent at trial. The Bankruptcy Court's March 12, 1991 order is included in Appendix C of the Petition.

Petitioner appealed to the United States District Court for the Northern District of Georgia, Rome Division. After extensive briefing, the District Court entered an order on January 31, 1992, affirming the Bankruptcy Court's determination in favor of Respondent. The District Court held that the Petitioner's arguments were not supportable based upon the factual, legal and equitable considerations of the case. The District Court also held that the existence of Respondent's claim as well as the measurement of the diminution in value of Respondent's collateral pursuant to 11 U.S.C. § 507(b) were to be determined according to federal equitable principles, *not* the Georgia MVSFA or the Georgia Uniform Commercial Code. The District Court's January 31, 1992 decision is included in Appendix B of the Petition.

Petitioner then appealed to the United States Court of Appeals for the Eleventh Circuit. After extensive briefing, as well as oral argument conducted on December 1, 1992 at Petitioner's request, the Court of Appeals on May 20, 1993 entered its opinion affirming the Orders of the District Court and the Bankruptcy Court. 991 F.2d 682 (11th Cir. 1993). The Court of Appeals expressly determined that Respondent was entitled to an administrative expense claim based upon a variety of factors, as stated in the opinion. The Court of Appeals further determined that Respondent's claim for administrative expenses under 11 U.S.C. § 507(b) was *not* a claim for a deficiency on the underlying contractual obligation that financed the Debtor's purchase of the collateral. The Court of Appeals' May 20, 1993 decision is included in Appendix A of the Petition.

Petitioner then sought further review from the Court of Appeals by filing a Petition for Rehearing and Suggestion of Rehearing En Banc. As circumscribed by 11th Cir.R. 35-3, the Petition for Rehearing En Banc was denied because Petitioner failed to establish that the Panel Opinion issued on

May 20, 1993 was in *direct conflict* with precedent of the Eleventh Circuit or the Supreme Court. As further circumscribed by 11th Cir.R. 35-3, the Petition for Rehearing before the Panel itself was also denied. The September 30, 1993 opinion of the Court of Appeals is reported at 4 F.3d 940 (11th Cir. 1993) and is included in Appendix D of the Petition.

STATUTORY PROVISIONS INVOLVED IN THIS CASE

The following statutes are pertinent to the consideration of the Petition: 11 U.S.C. § 362(d)(1); 11 U.S.C. § 503(b); and 11 U.S.C. § 507(b). These statutes are reprinted in Appendix E of the Petition.

STATEMENT OF THE CASE

Respondent adopts in substantial part the "Background" section of the Eleventh Circuit's May 20, 1993 opinion reported at 991 F.2d 682, 684-685 (11th Cir. 1993), copied in Appendix A of the Petition, pages 2a through 4a,[4] as well as the "Facts" section of the District Court's January 31, 1992 decision, copied in Appendix B of the Petition, pages 15a through 18a.[5]

While there are various facts that have been omitted or misstated by the Petitioner in his Statement of the Case, in the interest of brevity, Respondent will comply with Sup.Ct.R. 15.1 by limiting its remarks to the most substantial and oft-

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[4] The Court of Appeals' opinion contains a typographical error at page 2a, Appendix A of the Petition. The Court of Appeals' opinion refers to a March 3, 1993 consent order lifting the automatic stay that was entered into between Paccar Financial Corporation (Respondent's predecessor-in-interest) and Petitioner. The actual date of the consent order was March 30, 1993, the very day that Petitioner sought to convert the case to Chapter 7 of the Bankruptcy Code.

[5] The District Court's decision contains a typographical error at page 16a, Appendix B of the Petition. The District Court's decision refers to a Motion for Relief from Stay filed by Respondent's predecessor-in-interest, Paccar Financial Corporation, on March 30, 1987. The actual filing date of the Motion was March 20, 1987, less than one month after the bankruptcy case was filed on February 25, 1987.

repeated factual and legal mischaracterizations and omissions contained in Petitioner's Statement of the Case, as enumerated in the twelve (12) points outlined below:

(1) Petitioner repeatedly asserts that Respondent, through its predecessor-in-interest, Paccar Financial Corporation ("Paccar"), was attempting to seek authorization to exercise its "state law rights" with respect to its collateral. While it is true that Respondent, and its predecessor-in-interest, Paccar (collectively referred to hereafter as "Respondent"), were seeking to lift the automatic stay in order to repossess the collateral, there is no factual record in this case to establish that Respondent's primary goal was to "exercise its state law rights with respect to the collateral."

Indeed, for purposes of interpreting 11 U.S.C. § 507(b), the Bankruptcy Code provision at issue in this case, Respondent's goals under state law are completely irrelevant. Throughout this case, Respondent has not asserted a *deficiency* against the Petitioner pursuant to Georgia state law.

Rather, Respondent sought a superpriority administrative expense pursuant to 11 U.S.C. § 507(b) because of the *diminution in value* of its collateral during the pendency of the bankruptcy case and the inadequacy of adequate protection payments received.

(2) Petitioner alleges that he immediately consented to an order to allow Paccar to "foreclose its security interest in the aforesaid collateral in accordance with the laws of the State of Georgia or any other state in which the collateral is located."

In actuality, the March 30, 1988 consent order granted Paccar the "*right* to foreclose its security interest in the aforesaid collateral in accordance with the laws of the State of Georgia or any other state in which the collateral is located." (Emphasis supplied.) This language by its express terms was permissive, not mandatory, and it did not impose any additional obligations upon Paccar in connection with its disposition of the collateral.

Most significantly, Petitioner failed to advise this Court of additional language, contained in the very same order, that

granted Paccar relief from the automatic stay to obtain possession of the collateral and which provided, in pertinent part:

> The within order is . . . entered *without prejudice* to the Movant [Respondent] *in regard to Movant's right to assert an administrative claim in regard to the adequate protection payments which were not made by Debtor, and without prejudice to Movant's right to assert any other claims it may have against the Estate of Debtor.* (Emphasis supplied.) (BR.177-178).[6]

The referenced consent order was signed by the Petitioner and the attorney for the Creditors' Committee.

(3) Petitioner alleges that "Respondent asserted two claims against the Debtor. One was an alleged unsecured (deficiency) claim in the amount of $413,561.71. The other claim was a claim for a superpriority administrative expense in the exact same amount." Nothing could be further from the truth.

Throughout this case, beginning with Respondent's Administrative Expense Motion, Respondent has not asserted a *deficiency* against the Petitioner pursuant to the provisions of the Georgia MVSFA. A state law contractual deficiency claim, founded upon a pre-petition contract, is entirely different from a *diminution in value* claim asserted pursuant to 11 U.S.C. § 507(b). The latter arose subsequent to and as a direct consequence of the bankruptcy and was intended to compensate Respondent, a secured creditor, for the reduction in value to its collateral due to the imposition of the automatic stay pursuant to 11 U.S.C. § 362, and due to the insufficiency of adequate protection payments that it received.

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[6] The District Court record shall be cited to as "R-___-___-___" for volume number, document number, and the page number. Additionally, the Bankruptcy Court Record in this case is maintained in three separate volumes. The third volume received by the District Court contains the transcript of the full-day trial held by the Bankruptcy Court on February 26, 1991. The Bankruptcy Court trial transcript shall be cited to as "T.___" for page number. References to the Bankruptcy Court record contained in the other two volumes of exhibits will be cited by their Bankruptcy Court record number as "BR.___".

Contrary to the Petitioner's assertions, Respondent's predecessor-in-interest, Paccar, did *not* limit its total claim to $413,561.71. Indeed, Paccar timely filed a "Motion for Allowance of and Proof of Administrative Expense and Claim" ("Administrative Expense Motion"). (BR.182). The sums owing on Paccar's retail installment contracts/security agreements at the time that Paccar's Administrative Expense Motion was filed amounted to $413,561.71, subject to increase for allowed interest and attorney's fees accrued thereon up to a total of $465,861.40. (BR.185).

The Petitioner himself entered into a consent order on March 30, 1988 which by its express terms permitted Respondent to assert its administrative claim in bankruptcy. Also, at the very same hearing pursuant to which the consent order lifting stay was entered on March 30, 1988, the Petitioner concurrently filed his own Motion to Convert the case to a Chapter 7 liquidation proceeding. Consequently, it is inequitable for the Petitioner to *now* argue that compliance with the Georgia MVSFA is mandatory, especially when no benefit to the bankruptcy estate could have resulted from attempting to redeem the very same collateral that the Petitioner had already voluntarily and irrevocably abandoned in a Chapter 7 liquidation proceeding.

(4) The Petition, in the text accompanying footnote 5, also alleges that the Bankruptcy Court based its award pursuant to 11 U.S.C. § 507(b) upon the amount that Respondent paid to Paccar under the recourse obligation. This is also patently misleading.[7]

During the trial held before the Bankruptcy Court, counsel for Respondent established that the total diminution in value of Respondent's collateral amounted to approximately $489,614. (T.104). However, the Bankruptcy Court sought to

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[7] Petitioner improperly alleges that the amount Respondent paid to Paccar pursuant to its recourse obligation was, according to the District Court, "related to and corresponded with the amount of decrease in value of the collateral during the pendency of the case, a conclusion that was not made or considered by the Bankruptcy Court." Petitioner's assertions are not supported by the record.

equitably *limit* the award of Respondent's administrative priority claim pursuant to 11 U.S.C. § 507(b) to the $370,915.96 that it was required to tender to Paccar, its predecessor-in-interest, pursuant to a recourse obligation incurred as a consequence of the diminution in value to its collateral. According to the Bankruptcy Court, the recourse obligation was the best evidence of the damages incurred by Respondent as a result of the diminution in value to its collateral. This was because real dollars, a real loss, was incurred by Respondent from the recourse obligation, and the Bankruptcy Court determined that this was better evidence than the opinion testimony of the expert witnesses introduced by both parties.

While the Bankruptcy Court established that Respondent's collateral had clearly diminished in value due to the automatic stay during the pendency of the bankruptcy case, and that Respondent's claims clearly exceeded the $370,915.96 awarded as an administrative priority claim, the equitable limitation of the award to $370,915.96 was designed to prevent any "windfall" to Respondent. Consequently, contrary to the Petitioner's assertions, the Bankruptcy Court's award of an administrative priority claim to Respondent was not *based* upon this amount. Rather, the Bankruptcy Court intended to equitably *limit* the award to Respondent based upon the uncompensated diminution in value of its collateral which it contended amounted to approximately $489,614. The Bankruptcy Court stated the following:

> . . . One other point I want to make sure you understand, and I want it clear on the record, when I say, "Make you whole," I'm talking about that period during the administration of the Chapter 11, point A to point B where your collateral was actually being used for the benefit of all creditors. And that is where you suffered the loss.
>
> Now, I don't have to make you whole with respect to your general breach of contract claim . . . That is not entitled to the priority status. (T.109).

However, the Bankruptcy Court refused to comment on the validity of such a general unsecured "deficiency" claim, and it determined that such an unsecured claim would be

subject to objection by the Petitioner, pursuant to any applicable state law, including the MVSFA, precisely because such a general unsecured claim would be the type of "deficiency" that the MVSFA was expressly intended to address. (T.200). Accordingly, Respondent has not, at any point in the proceedings below, attempted to pursue such a contractual deficiency claim because of the application of the Georgia MVSFA to such claims.

(5) Petitioner alleges, "Despite the Debtor's failure to timely comply with the adequate protection arrangement, Paccar did not aggressively prosecute its remedies under the Bankruptcy Code." These assertions are patently untrue. The record will reflect that Respondent asserted and protected its rights in its collateral used by the Debtor and diligently attempted to collect amounts due from the Debtor on a timely basis, at every stage of the case. *See* Respondent's "Brief of Appellee" filed with the District Court, pages 4-7 (R-1-2-4/7), and Respondent's "Brief in Response to Appellant's Reply", pages 8-9 (R-2-7-8/9).

Further, Paccar filed its Motion for Relief from Stay and for Adequate Protection on March 20, 1987, *less than one month after Debtor commenced its bankruptcy case on February 25, 1987.* This action by Respondent's predecessor-in-interest is representative of the vigilant and ongoing efforts which Respondent has made in attempting to secure its rights throughout the entire case.

(6) The Petition at footnotes 5 and 11 alleges that Respondent failed to establish the value of the collateral in question. This argument is flawed, overly simplistic, and overlooks the voluminous evidence established by Respondent at trial on February 26, 1991.

At trial, the Bankruptcy Court took the position that if Respondent established a diminution in the value of its collateral, the loss would be measured by the difference between the fair market value of the property at the time that the Debtor filed its Chapter 11 petition and the time that the automatic stay was lifted, less adequate protection payments previously made by the Debtor. (T.24, 33-35).

Respondent's expert witness testified extensively about the damages that occurred to the tractors due to the automatic stay during the pendency of the bankruptcy case. Respondent also testified about the fair market value of the tractors at issue as of the time the Chapter 11 bankruptcy was filed. The valuation was made based upon the particular specifications for each of the individual tractors at issue. The cumulative value of the tractors at the time that the bankruptcy was filed was $575,000, based upon criteria established in a nationally recognized and authoritative valuation publication called the "Blue Book". (T.45-47).

The Bankruptcy Court considered and rejected the Petitioner's argument that on February 25, 1987, the day that the Debtor filed its Chapter 11 bankruptcy case, Respondent should have physically inventoried and inspected all twenty-six (26) tractors on that date (T.114). The Bankruptcy Court noted that such a requirement, as a practical matter, would have been impossible to administer. This was primarily due to the fact that the vehicles were constantly travelling throughout different parts of the country, that it would impose an undue financial burden on the Debtor, that it was not called for by the Bankruptcy Code, and that no one could possibly physically inspect all or necessarily any of the vehicles on or around those dates. (T.114-123). The Bankruptcy Court indicated that for the foregoing reasons, such a task as a matter of course is never performed. (T.115).

Petitioner goes to great lengths to try to impeach Respondent's reliance upon the Blue Book as a basis for determining the value of the tractors at the time of the Chapter 11 filing. This argument completely overlooks the fact that *Petitioner's own expert witness used the Blue Book to determine the value of the tractors at the time that the Chapter 11 bankruptcy was filed.* (T.127-128).

The Bankruptcy Court determined that Respondent had met its burden of proof:

> What if we just stop everything right now, have evidence that the trucks in question, whatever they are, tractors, were worth $575,000 on day one. And when the things are brought back in, it was a basket

> case. It ultimately sold for $60,000 scrap value. So, isn't that some evidence that I could pin my hat on and hang my hat on and say that they got a diminution in value here? (T.122-123).

The District Court also determined that the factual findings of the Bankruptcy Court were supported by the record and that such findings were not clearly erroneous. "These factual findings have support in the record and this Court cannot say that they are clearly erroneous." (R-2-10-20); Appendix B of the Petition, pages 28a through 29a. Consequently, there was ample evidence to support the Bankruptcy Court's award and the District Court's affirmance thereof.

(7) The Petition at footnote 3 and accompanying text alleges that Paccar failed to send the required notices under the Georgia MVSFA, O.C.G.A. § 10-1-36, on a timely basis and failed to comply with the "commercially reasonable" sale requirements under the Georgia Uniform Commercial Code, O.C.G.A. § 11-9-504(3). Specifically, the Petitioner asserts that there was no evidence that the public sale of the collateral was advertised. Even though these allegations are completely irrelevant to the equitable basis of Respondent's claims under 11 U.S.C. § 507(b), Petitioner's allegations ignore the facts. The collateral was advertised by Paccar for sale, and this was acknowledged by the Bankruptcy Court at the trial on February 26, 1991. (T.81-82).

Moreover, Paccar disposed of the tractors at public sale only after giving prior written notice by certified mail to all interested parties of the Debtor's right to redeem the collateral prior to its disposition, and of Paccar's intention to assert its right to pursue the Debtor for any resulting deficiency. (T.64). These allegations have relevance only if the basis for Respondent's claims is grounded upon state law, which it is *not*.

(8) Contrary to the Petitioner's assertions that the tractors were returned to Paccar shortly after the entry of the March 30, 1988 consent order, "during the end of March and the beginning of April of 1988," the vehicles were not collected or made readily available to Paccar by the Petitioner or the Debtor. (T.61-62). Paccar had to locate and physically

reclaim the tractors over a number of weeks and months subsequent to the entry of the above-referenced order. In fact, the tractors were located across at least two states. (T.51). Though a number of the tractors were located and reclaimed by Paccar within a month or so after the entry of the consent order (BR.184), at least one of the tractors was returned as late as August 13, 1988. (T.53).

(9) Petitioner alleges that the Court of Appeals determined that "the Debtor's use of its own property postpetition created an independent claim in favor of Respondent . . . " This argument conveniently overlooks the fact that the tractors used by the Debtor were financed by Paccar and were subject to a first priority security interest held by Paccar in those tractors. Further, the only reason Paccar did not obtain the immediate return of those tractors after Debtor filed its bankruptcy petition was because an adequate protection order was given to Paccar after it filed its motion to lift stay, less than a month after Debtor commenced its Chapter 11 bankruptcy proceeding.

Indeed, the Court of Appeals accurately made the following observation:

> . . . [T]his case does involve a post-petition transaction beneficial to Debtor's estate rather than a mere continued use of the truck by Debtor. Paccar consented to forgoing foreclosure on its secured collateral only after negotiating for adequate protection payments in return for leaving the trucks in Debtor's possession.[8]

(10) Petitioner further alleges that the District Court determined that the Bankruptcy Code and federal equitable principles "created claims in favor of Respondent even if the claims otherwise did not exist under applicable substantive law." Petitioner again disregards the District Court's determination that an administrative expense claim brought pursuant to 11 U.S.C. § 507(b) is "a creature of the Bankruptcy

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[8] 991 F.2d 682, 686 (11th Cir. 1993); Appendix A of the Petition, pages 6a through 7a.

Code and its existence can be attributed directly to the policy decisions made by Congress." (R-2-10-13); Appendix B of the Petition, page 23a. The District Court held that such a claim was not a "deficiency" claim subject to determination according to state deficiency law statutes. *Id.* The District Court in fact concluded:

> [Respondent's] administrative expense claim is thus part of a carefully balanced system of benefits and burdens created by Congress. *The claim arises from the unique circumstances of a bankruptcy case and is legally distinct from any nonbankruptcy theory.* It is not a deficiency claim. (Emphasis supplied). (R-2-10-15); Appendix B of the Petition, page 25a.

(11) The Petition at footnote 2 alleges that the Court of Appeals mistakenly asserted that the "Trustee," i.e., the Petitioner, benefitted from the use of Respondent's collateral. However, throughout its May 20, 1993 opinion, the Court of Appeals clearly recognized that the Debtor-in-Possession and the bankruptcy estate, not the Petitioner, actively used and caused the diminution in value to Respondent's collateral. Indeed, the Court of Appeals' occasional use of the term "Trustee", at least in the context of the Debtor-in-Possession's operation of its business in a Chapter 11 context, is proper. 11 U.S.C. § 1107(a) provides in pertinent part that a Debtor-in-Possession shall "have all the rights . . . and powers, and shall perform all the functions and duties . . . of a trustee serving in a case under this chapter."

(12) Petitioner alleges that Respondent's predecessor-in-interest, Paccar, entered into a consent order requiring Debtor to make monthly payments of $18,661.25. In fact, the monthly payments were $19,651.40. Petitioner also alleges that the monthly payments were subsequently reduced to $15,890.80 after three (3) of the twenty-six (26) tractors were paid in full by the Debtor. In fact, the monthly payments were reduced to $16,680.95. The numbers referred to by the Petitioner are possibly based upon typographical errors contained in pleadings filed very early in the case by Paccar prior to Respondent's involvement. However, Respondent corrected this information in pleadings filed prior to the February 26,

1991 trial by the Bankruptcy Court, and this corrected information was also contained in every brief filed by Respondent with the District Court and Court of Appeals as well.

The referenced consent order was an *adequate protection order* which was entered on May 19, 1987 pursuant to 11 U.S.C. § 362(d)(1), *not* 11 U.S.C. § 361. Though Petitioner alleges that $108,500 in adequate protection payments were made by the Debtor during the course of the Chapter 11 bankruptcy proceeding, Petitioner fails to mention Respondent's entitlement to the additional $67,715.53 in unpaid adequate protection payments which Respondent was awarded pursuant to the Bankruptcy Court's May 19, 1987 Adequate Protection Order.

SUMMARY OF ARGUMENT

Petitioner has failed to establish, pursuant to Sup.Ct.R. 10.1, the basis for granting his Petition for Writ of Certiorari. Petitioner has failed to demonstrate *any* conflict between the opinion of the Eleventh Circuit Court of Appeals and any decision of the Supreme Court, the Eleventh Circuit, or another Circuit Court of Appeals. Indeed, as circumscribed by 11th Cir.R. 35-3, the Petition for Rehearing En Banc filed by Petitioner to the Eleventh Circuit Court of Appeals was denied for these reasons.

Petitioner has failed to establish any meritorious argument for consideration by this Court. Petitioner claims that this case "involves important issues of federal bankruptcy law and its relationship to state law." However, this case does not involve any interplay between federal bankruptcy law and state law, because state law is not applicable to the type of administrative priority award that was made to Respondent pursuant to 11 U.S.C. § 507(b).

While state law may be relevant to the determination of causes of action based upon a pre-bankruptcy transaction between a creditor and the debtor, state law has no application or relationship to 11 U.S.C. § 507(b), which *only* arises due to a new relationship forged between a secured creditor and the debtor *after* (1) a bankruptcy case has been filed; (2) a

secured creditor has moved for and obtained an adequate protection order pursuant to 11 U.S.C. § 362(d)(1) or such other provision of the Bankruptcy Code; and (3) there has been a diminution in value to the secured creditor's collateral which was not fully compensated for by the negotiated adequate protection payments made pursuant to the Bankruptcy Code. Respondent's rights pursuant to 11 U.S.C. § 507(b) arose as a consequence of the bankruptcy case, not because of state law.

The Petitioner has failed to cite any case on point showing that the measurement of a diminution in value claim pursuant to 11 U.S.C. § 507(b) is dependent on state law. This is precisely so because Petitioner's reliance upon the MVSFA, O.C.G.A. § 10-1-36, and the Georgia Uniform Commercial Code, O.C.G.A. § 11-9-504, in this instance is inapposite and misplaced.

The Petitioner ignores that Respondent's Administrative Expense Motion did not seek to assert a deficiency claim. Had Respondent sought to assert a *deficiency* against the Debtor, such a deficiency would have been calculated by referring to the remaining sums outstanding on the retail installment contracts/security agreements involved in this case and deducting therefrom the proceeds obtained at public sale.

Instead, Respondent sought and obtained a superpriority administrative expense pursuant to Bankruptcy Code Section 507(b) due to the *diminution in value* of its collateral during the pendency of the case and the inadequacy of adequate protection payments received, without making *any* reference to the remaining sums outstanding on the retail installment contracts/security agreements involved in this case. Respondent has, in fact, not attempted to assert a contractual deficiency claim in the proceedings below precisely because of the application of the Georgia MVSFA to such claims.

Further, it is inequitable for the Petitioner to *now* argue that compliance with the MVSFA is mandatory when the Petitioner entered a consent order on March 30, 1988 which by its express terms permitted Respondent to assert its administrative claim in bankruptcy. Indeed, at the very same hearing pursuant to which the consent order lifting stay was entered

on March 30, 1988, the Petitioner concurrently filed his own Motion to Convert the case to a Chapter 7 liquidation proceeding.

Consequently, no benefit to the bankruptcy estate could have resulted from attempting to redeem the very same collateral that the Petitioner had already voluntarily and irrevocably abandoned, particularly in a Chapter 7 liquidation proceeding.

With respect to the factual issues considered, Respondent proved during the trial conducted by the Bankruptcy Court on February 26, 1991, that its collateral had diminished in value by at least approximately $489,614 during the pendency of the Chapter 11 case in excess of the amount of adequate protection payments which it received, and that the loss was in fact caused by the automatic stay.

This sum was proven at trial before the Bankruptcy Court. The equitable limitation of the award to $370,915.96 was designed to prevent any "windfall" to Respondent. Consequently, contrary to the Petitioner's assertions, the Bankruptcy Court's award of an administrative priority claim to Respondent was not based upon this amount. Rather, it served to equitably *limit* the award to Nalley based upon the diminution in value of its collateral which it contended amounted to approximately $489,614.

The Court of Appeals and the District Court determined that there was sufficient evidence proven by Respondent on the record to determine that the Bankruptcy Court was *not* clearly erroneous in its factual determinations and that the record provided sufficient evidence to fully affirm the Bankruptcy Court's award to Respondent of a priority administrative claim pursuant to 11 U.S.C. § 507(b).

Unlike the other types of creditors referred to by Petitioner, Respondent gave new value and agreed to forego its rights in its collateral only after it was given assurances by virtue of the adequate protection order entered by the Bankruptcy Court that it would be made whole for any diminution in the value of its collateral. The parties made a deal in open court, the Bankruptcy Court blessed the deal, and now the Petitioner seeks to back out of the deal.

ARGUMENT: REASONS FOR DENYING THE WRIT

1. THE PETITIONER HAS FAILED TO ESTABLISH A SUFFICIENT BASIS PURSUANT TO SUP.CT.R. 10 TO JUSTIFY A GRANT OF CERTIORARI BY THE SUPREME COURT.

A. Petitioner Has Failed to Establish That There Is *Any* Direct Conflict Between The Holding of The Eleventh Circuit Court of Appeals and A Decision of This Court or Another Circuit.

As has been discussed in the Summary of Argument, *supra*, Petitioner has failed to identify *any* direct conflict between the case on appeal and a decision of the Supreme Court or any other Circuit Court of Appeals.

Further, the Petitioner has failed to cite any case on point showing that the measurement of a diminution in value claim pursuant to 11 U.S.C. § 507(b) is dependent on state law. This is precisely because Petitioner's reliance upon the MVSFA, O.C.G.A. § 10-1-36, and the Georgia Uniform Commercial Code, O.C.G.A. § 11-9-504(3), are inapposite and misplaced.

B. Petitioner's Inequitable Arguments are Flawed and Defeat the Very Purpose of Chapter 11 of the Bankruptcy Code to Promote the Rehabilitation of A Debtor in Bankruptcy.

The Bankruptcy Court summed up the tenor of the arguments and positions asserted by the Petitioner as follows:

> THE COURT: The problem I have with your position, Mr. Nason [counsel for Petitioner], is if I really interpreted the statute [11 U.S.C. § 507(b)] and the elements of that statute the way you are interpreting them, you would never get a Chapter 11 beyond day one. This is the truth. This is not what Congress intended. Congress did not make – Congress did not intend that – to make it extremely difficult for lenders to come forward in a Chapter 11 and either negotiate adequate protection or to

> lend fresh cash with cash collateral orders. The object of Chapter 11 is to keep the wheels of commerce turning. It's to keep the business going to try to salvage an on-going business. *If I agreed with your interpretation, and I realize it's pure hindsight, I would throw up so many roadblocks to a Chapter 11, you would never get one past day one. I might as well just abort it and put it into Chapter 7. No lender in its right mind would ever come near the Chapter 11 court voluntarily and say, "Here's fresh cash or here's an agreed upon Adequate Protection Order."* (Emphasis supplied.)
>
> Mr. Nason, that is not the way Chapter 11 is supposed to operate.
>
> MR. NASON: Yes, sir, I can understand what Your Honor is saying . . . (T.118-119).

The District Court also formed its own opinion of the Petitioner's inequitable arguments and positions as follows:

> In the view of this Court . . . *[Petitioner's] argument is based upon flawed conceptions of both Georgia's law of foreclosure and administrative claims in bankruptcy.* This Court finds that the alleged inadequacies in [Respondent's] post repossession conduct does not negate the existence of [Respondent's] claim against the debtor's estate. Moreover, this Court is not persuaded that an administrative expense claim can be considered a deficiency claim. (Emphasis supplied.) (R-2-10-12); Appendix B of the Petition, page 23a.

The Court of Appeals likewise took issue with the arguments put forth by Petitioner:

> At the outset, we must clarify the nature of [Respondent's] claim in order to focus on the issues actually involved in this case. The [Petitioner] argued both in his briefs and at oral argument that [Respondent's] claim is barred by Paccar's alleged failure to comply with foreclosure laws of the State of Georgia. The [Petitioner] contends that because

> Paccar failed to carry out foreclosure and sale of the collateral according to the terms of the Georgia Motor Vehicle Sales Finance Act and the Georgia Commercial Code, [Respondent], as successor-in-interest, cannot assert a claim against Debtor's estate based on the loss suffered by Paccar when the sale of the collateral produced less than the balance due on the purchase money notes.
>
> *This argument misses the point. A claim for administrative expenses under 11 U.S.C. § 507(b) is not a claim for a deficiency on the underlying obligation which financed Debtor's purchase of the collateral.* The [Petitioner] appears to be correct in asserting that compliance with state law controls a creditor's right to claim, against the bankruptcy estate, a deficiency on a contract after foreclosure of a lien. *We need not reach this question, however, because this case does not present that issue. Instead of a contract deficiency claim, [Respondent] asserts a claim for administrative expenses for the value of goods furnished to the bankruptcy estate after imposition of the automatic stay . . .* (Emphasis supplied.) 991 F.2d 682, 685 (11th Cir. 1993); Appendix A of the Petition, page 4a.

C. Petitioner Is Attempting to Deprive Secured Creditors in Bankruptcy of the Right to Protect the Value of Their Collateral During the Imposition of the Automatic Stay in Bankruptcy.

Petitioner fallaciously argues that state law creates *all* claims between a creditor and debtor in bankruptcy, and that claims should be treated the same in federal and state courts,[9] citing *Butner v. United States*, 440 U.S. 48 (1979), in support of this assertion. However, *Butner* addressed the question of whether a pre-petition security interest in real property extends to post-petition rents and profits derived from the

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[9] Petition at pages 8 and 13.

property. *Butner* did not even contemplate or attempt to address the post-petition creation or existence of administrative priority claims in bankruptcy based upon a debtor's use of a secured creditor's collateral and the resulting diminution in value of the collateral due to the imposition of the automatic stay in bankruptcy.

Petitioner also argues that the impact of the Court of Appeals' opinion will be adverse and far reaching if not reversed. To the contrary, reversing the lower courts' holdings in this case would unravel those provisions of the Bankruptcy Code specifically designed to induce secured creditors into continuing to transact business with a debtor-in-possession and to continue furnishing goods and services to the debtor in order to rehabilitate the debtor's business in Chapter 11.

The message that would be sent throughout the secured creditors' community by reversing the Eleventh Circuit Court of Appeals would be to inform secured creditors that under no circumstances will they be made whole for their losses when their collateral diminishes in value in excess of the adequate protection payments received. Petitioner wants to deprive secured creditors such as Respondent of the benefit of their bargain retroactively. Petitioner seeks to use state law as a sword to deprive secured creditors who enter into post-petition transactions in order to rehabilitate the Debtor from recovering for the unanticipated reduction in value to their collateral during the pendency of the bankruptcy case.

Petitioner argues that other Chapter 11 administrative expense claimants will not be paid in full, and that pre-petition claimants will not receive anything. However, the Respondent was induced to do business with the Debtor *after* the bankruptcy case was filed, and unlike the pre-petition and post-petition unsecured creditors referred to by Petitioner, Respondent had valuable collateral that it was entitled to repossess. Due to the imposition of the automatic stay in bankruptcy and the prompt entry of an adequate protection order after the bankruptcy case was initiated, Respondent was induced into refraining from repossessing its valuable collateral in exchange for the guarantee of satisfactory adequate protection payments.

Consistent with this analysis, the Court of Appeals determined the following:

> . . . [T]his case does involve a post-petition transaction beneficial to Debtor's estate rather than a mere continued use of the trucks by Debtor. Paccar consented to forgoing foreclosure on its secured collateral only after negotiating for adequate protection payments in return for leaving the trucks in Debtor's possession. Facing a similar claim of administrative expenses for failed adequate protection, the court in *In re Mutschler*[10] stated:
>
> Section 503(b)(1)(A) of the Code entitles a creditor to administrative priority for any claim representing an actual and necessary cost of preserving the estate. Section 507(b) is an adjunct to the adequate protection alternative set forth in section 361 . . . Adequate protection is a means of preserving a creditor's interest in secured collateral subject to post-petition use by the debtor. *Presumably such use is desired by the debtor and is contributing to the reorganization effort. Otherwise, the debtor would doubtless return the collateral and forgo providing adequate protection. This beneficial use by the debtor is normally "paid for" by the adequate protection.* Where adequate protection becomes inadequate or otherwise fails and the use nonetheless continues, section 507(b) comes into play by covering the creditor's unprotected interest by according it priority administrative expense status. (emphasis added) . . . 991 F.2d 682, 686 (11th Cir. 1993); Appendix A of the Petition, pages 7a through 8a.

Accordingly, Petitioner has chosen to disregard that Respondent's award pursuant to 11 U.S.C. § 507(b) was based upon its entitlement to adequate protection payments which were insufficient to fully compensate it for the diminution in

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[10] 45 B.R. 494, 496 (Bankr. D.N.D. 1984).

value to its collateral. This award was based upon federal equitable principles and the Bankruptcy Code, *not* state law.

2. THE COURTS BELOW PROPERLY RULED UPON THE ISSUES ADJUDICATED BETWEEN PETITIONER AND RESPONDENT, THEREBY JUSTIFYING THE AWARD OF $370,915.96 PURSUANT TO 11 U.S.C. § 507(b).

A. Petitioner Incorrectly Asserts that the Origin of All Rights Established Under the Bankruptcy Code Are Derived from State Law.

Petitioner contends that "The Bankruptcy Code is essentially a prioritizing scheme" and that "Claims against a bankruptcy estate are created and determined under state law." Petitioner cites two cases, *Matter of Winslow,* 39 B.R. 869 (Bankr. N.D.Ga. 1984), and *In re Kahihikolo,* 807 F.2d 1540 (11th Cir. 1987) (containing dicta referring to the *Winslow* case), allegedly for the proposition that "[o]nce the automatic stay is lifted, the parties' rights revert to those under state law."[11]

However, the *Winslow* case dealt with a creditor's attempt to assert a general unsecured *deficiency* claim against the estate after the repossession and sale of Debtor's vehicle in which it had a security interest. That case did not involve an adequate protection order. It also did not deal with the ultimate insufficiency of those adequate protection payments to offset the diminution in value of the secured creditor's collateral and that creditor's subsequent claim for a super-priority administrative expense pursuant to 11 U.S.C. § 507(b).

Petitioner argues that pursuant to the Georgia MVSFA, Respondent lost all rights to a deficiency claim against the Debtor or the bankruptcy estate. In support of this proposition, Petitioner improperly cites *Redman Industries v. Tower*

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[11] Petition at page 10.

Properties, Inc., 517 F. Supp. 144 (N.D.Ga. 1981).[12] That case concerned the Georgia real estate mortgage "confirmation statute", which was designed to protect debtors from deficiency judgments obtained by mortgage lenders in the event their *real property* has been sold at a foreclosure sale for less than fair market value. *Redman* is inapposite to the facts of the instant case because (1) personal, not real property was at issue in the instant case; (2) Respondent's award, made pursuant to 11 U.S.C. § 507(b), was based upon the diminution in value which occurred to Respondent's collateral subsequent to the imposition of the automatic stay in bankruptcy, not upon a state law deficiency claim; and (3) Respondent's collateral was not sold at or below its market value.

Petitioner also alleges that "[u]nder § 558 of the Bankruptcy Code, the estate has the benefit of any defenses that would be available to the debtor as against any entity."[13] This argument is superfluous, since the March 30, 1988 consent order which granted Paccar relief from the automatic stay to obtain possession of the collateral was made when the Petitioner had already been appointed a Trustee in the case. This consent order was entered by Petitioner himself and provided, in pertinent part:

> The within order is . . . entered *without prejudice* to the Movant *in regard to Movant's right to assert an administrative claim in regard to the adequate protection payments which were not made by Debtor, and without prejudice to Movant's right to assert any other claims it may have against the Estate of Debtor*. (Emphasis supplied.) (BR.177-178).

11 U.S.C. § 558 is therefore inapplicable, because at the time the consent order was entered, the Debtor was neither the party which dealt with Respondent nor was even possessed at that time with the right to object to the disposition of the vehicles made the subject of the Petition.

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[12] Petition at page 10, footnote 9, and at page 20. Petitioner mistakenly refers to this case throughout his Petition as *Redmond Industries, Inc. v. Tower Properties, Inc.*, 517 F.Supp. 144 (N.D.Ga. 1981).

[13] Petition at page 10, footnote 10, and at page 21.

Petitioner also refers to 11 U.S.C. § 502(b)(1)[14] in a further attempt to contest Respondent's award pursuant to 11 U.S.C. § 507(b). Not only is the application of 11 U.S.C. § 507(b) *not* affected by 11 U.S.C. § 502(b)(1), but 3 *Collier on Bankruptcy* ¶ 502.02, p. 502-29 (15th ed. 1993), also states, "This is not to suggest that the claim is allowed only for the value of the collateral. It is allowed in the full amount that it is valid."

Finally, Petitioner contends that "Respondent has implicitly recognized that state law is not irrelevant", and alleges that Respondent limited its unsecured claim to $413,561.71.[15] *See* numbered paragraph (3) of Respondent's Statement of the Case in this Brief, *supra*, which thoroughly addresses and disproves Petitioner's contentions in this regard. Contrary to the Petitioner's assertions, Paccar did *not* limit or "cap" its total claim to $413,561.71.

Petitioner concludes his dubious argument by alleging that " . . . § 507(b) is designed to make a creditor 'whole' if it receives everything it is entitled to under its loan documents and state law."[16] Petitioner fundamentally disregards the nature of diminution in value claims awarded pursuant to 11 U.S.C. § 507(b). They are not made pursuant to the diminution in value or cancellation of the underlying loan documents or pursuant to the application of an anti-deficiency statute. Rather, they are made pursuant to the diminution in value of the *collateral* which constitutes the security for a debtor's obligation to a secured creditor.

B. Respondent's Award Pursuant to 11 U.S.C. §§ 507(b) and 503(b) Was Based Upon Debtor's Ability to Use and Benefit from Respondent's Collateral in Exchange for Adequate Protection.

The Petitioner alleges that Respondent's § 507(b) award did not arise because of the diminution in value of its collateral, but rather "under its prepetition notes with the

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[14] Petition at page 21.

[15] Petition at page 13, footnote 14, and accompanying text.

[16] Petition at pages 13-14.

Debtor."[17] Petitioner is unable to support this implausible and misguided argument other than by asserting that Respondent did not provide any benefit to the Debtor that would justify an award for the "actual, necessary costs and expenses of preserving the estate" pursuant to 11 U.S.C. § 503(b). Petitioner particularly relies upon two cases to support these assertions, *In re Advisory Information and Management Systems, Inc.*, 50 B.R. 627 (Bankr. M.D.Tenn. 1985),[18] and *In re James B. Downing & Co.*, 94 B.R. 515 (Bankr. N.D.Ill. 1988).[19]

However, Petitioner's tortuous logic is contrary to the holding of every court below, especially the Court of Appeals, which expressly recognized the benefit to the estate conferred by Respondent's collateral. Indeed, the Court of Appeals addressed Petitioner's contentions as follows:

> The cases relied upon by the [Petitioner] are readily distinguishable from the case at bar . . .
>
> [5] Unlike the creditors in *Advisory Information and Management Systems* and *James B. Downing*, [Respondent's] predecessor-in-interest utilized the statutory procedures provided for protection of its collateral in the possession of Debtor. [Respondent] does not proffer § 503 as an alternative to adequate protection of its secured claim. *Instead of merely sitting back and allowing Debtor to continue using the tractors, Paccar asserted its undeniable right to repossession and agreed to forgo repossession only after and because Debtor consented to paying adequate protection. Therefore, [Respondent's] administrative expense claim is not barred under the inaction theory which controlled in Advisory Information and Management Systems* and *James B. Downing*. (Emphasis supplied.) 991 F.2d 682, 687 (11th Cir. 1993); Appendix A of the Petition, pages 8a through 10a.

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[17] Petition at pages 12-14.

[18] Petition at pages 12, 16-17.

[19] Petition at page 14.

Petitioner also cites to *In re Subscription Television of Greater Atlanta*, 789 F.2d 1530 (11th Cir. 1986),[20] and reiterates the same tired "benefit to the estate" argument. However, the Court of Appeals distinguished *In re Subscription Television of Greater Atlanta* as follows:

> The debtor in the case at bar enjoyed more than mere potential post-petition use of collateral. *Rather than entertaining a speculative benefit, the Trustee [Debtor] actively used Paccar's collateral throughout its post-petition possession. This is not disputed. The reasoning of Subscription Television,* therefore, leads to the conclusion that [Respondent] is entitled to an administrative expense priority because the Trustee [Debtor] actually used the collateral to the benefit of the debtor's estate. Because this case does not involve a debtor's potential use of collateral, the [Petitioner's] reliance on *Subscription Television* is misplaced. (Emphasis supplied.) 991 F.2d 682, 687-688 (11th Cir. 1993), Appendix A of the Petition, pages 10a through 11a.

The Court of Appeals' analysis is entirely correct, since Debtor's use of Respondent's collateral, the over-the-road tractors, was the *sine qua non* of Debtor's business, and it is inequitable for the Petitioner to now argue that Debtor's ability to use Respondent's collateral during the Chapter 11 bankruptcy did not provide new value or a benefit to the estate. The fact that the Debtor entered into the Adequate Protection Order with Respondent (Paccar) is testimony to that value and benefit conferred upon the Debtor and the bankruptcy estate.

C. The Statutory History and Case Law Interpreting 11 U.S.C. §§ 507(b) and 361(3) Expressly Establish that the Former Is Neither Controlled Nor Limited by the Latter.

The Petition, at pages 15 through 21, ineffectively attempts to show that some type of conflict exists between 11

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[20] Petition at page 17.

U.S.C. §§ 507(b) and 361(3). This novel argument was first raised in earnest by Petitioner in his Reply Brief filed with the Eleventh Circuit Court of Appeals.

Petitioner's arguments concerning the interplay between 11 U.S.C. §§ 507(b) and 361(3) demonstrate a profound disregard for the statutory and case history of both of these provisions. The Court of Appeals, in its September 30, 1993 opinion[21], denied Petitioner's Motion for Rehearing and Suggestion of Rehearing En Banc based upon these arguments.

The September 30, 1993 opinion of the Court of Appeals clearly and succinctly dispatched Petitioner's arguments concerning 11 U.S.C. § 361(3) along with Petitioner's other arguments. The Court of Appeals elaborated upon the legislative history of these provisions and accompanying case law pertaining thereto in support of its denial of Petitioner's Motion for Rehearing and Suggestion of Rehearing En Banc.

Additional legislative history is found at 124 Cong. Rec. H 11092 (Sept. 28, 1978), which provides in pertinent part:

> Section 361(4) of H.R. 8200 as passed by the House is modified in section 361(3) of the House amendment to indicate that the court may grant other forms of adequate protection, other than an administrative expense, which will result in the realization by the secured creditor of the indubitable equivalent of the creditor's interest in property . . . Adequate protection of an interest of an entity in property is intended to protect a creditor's allowed secured claim. *To the extent the protection proves to be inadequate after the fact, the creditor is entitled to a first priority administrative expense under section 507(b).* (Emphasis supplied.)

Both 11 U.S.C. §§ 507(b) and 361(3) took effect on October 1, 1979 when the present Bankruptcy Code became effective. Based upon the referenced legislative and case

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[21] 4 F.3d 940 (11th Cir. 1993), Appendix D of the Petition, pages 35a through 37a.

histories of these provisions, it is disturbing but not unexpected that Petitioner should choose to ignore this background in arguing that these provisions are somehow incompatible. Presumably, Congress was aware of what it was doing when it enacted these provisions of the Bankruptcy Code at the same time.

D. The Concept of "Equality of Distribution" Advocated By Petitioner Pertains to Unsecured Creditors Who Have Not Been Required to Place Collateral At Risk During the Pendency of the Debtor's Chapter 11 Case.

Petitioner relies on the principle of "equality of distribution" as a talisman to be invoked against Respondent's administrative priority claim created pursuant to 11 U.S.C. § 507(b). By arguing this analysis, Petitioner is attempting to deny Respondent the benefit of its bargain, namely its entitlement to a priority administrative claim for the diminution in value to its collateral as a consequence of the imposition of the automatic stay in bankruptcy.

Equality of distribution is a concept used in bankruptcy analysis to distribute funds equally among unsecured creditors. What the Petitioner materially omits from the equation is that unlike Respondent and its predecessor-in-interest, Paccar, the Debtor's unsecured creditors were neither required to tender any additional funds nor contribute anything of value to the Chapter 11 bankruptcy estate post-petition. The Bankruptcy Court recognized this distinction and stated the policy of Congress with respect to the concept of equality of distribution as follows:

> THE COURT: The other creditors have to pay because Congress said – this is the congressional intent, "We," meaning Congress, "We want to facilitate a reorganization. We want all the creditors to share the risks." Now, we have one special creditor who has got a lien on this type of property, tractors, trailers. Okay. What Congress is saying in Section 507 is, "Look, if we are going to force that secured

> creditor to lie still while the debtor uses the property that is depreciating because the judge is going to keep that stay in effect, we are going to have to furnish adequate protection." And if an adequate protection is not sufficient to make that creditor whole, meaning make him go back to day one and make him whole, then all the creditors have to share that risk because that one creditor is going to be elevated to a priority administrative status. (T.119-120).

Petitioner also cites to *Shapiro v. Saybrook (In re Saybrook Manufacturing Co., Inc.)*, 963 F.2d 1490 (11th Cir. 1992)[22] for the proposition that a pre-petition secured creditor cannot obtain a priority claim over other similarly situated claimants. However, the *Saybrook* opinion dealt with a pre-petition secured creditor who attempted to "bootstrap" its claim in bankruptcy by a cross-collateralization provision that allowed its post-petition financing of the Debtor to not only secure that creditor's post-petition claim but its pre-petition claims as well.

The Eleventh Circuit's analysis of Respondent's claim, pertaining to the diminution in value of its collateral, renders the *Saybrook* opinion irrelevant to the facts of the instant case. Contrary to the Petitioner's assertions, Respondent did not obtain an administrative priority claim "over similarly situated claimants." Rather, Respondent suffered a unique loss occasioned by the failure of negotiated post-petition adequate protection payments to compensate adequately for the diminution in value of its collateral.

Petitioner also argues that *Vanston Bondholders Protective Committee v. Green*, 329 U.S. 156, 162-163, 67 S. Ct. 237, 240 (1946),[23] supports his argument concerning "equality of distribution." However, that case and its progeny expressly hold that in determining what claims are allowable and how the Debtor's assets are to be distributed are *not* dependent on the law of the state

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[22] Petition at pages 17-18.

[23] Petition at pages 19-20.

where the bankruptcy court is located. The bankruptcy court must administer and enforce the Bankruptcy Code in accordance with the authority granted by Congress to determine how and what claims shall be allowed under *equitable principles.*[24]

The *Vanston* decision held that the question of what claims are valid and subsisting obligations against the Debtor, in connection with those *existing at the time a bankruptcy petition is filed*, may be determined by reference to state law in the absence of overruling federal law.

The case at bar, does not involve the law of the State of Georgia precisely because Respondent's § 507(b) administrative priority claim pursuant arose *after* the bankruptcy petition was filed and as a direct consequence of the imposition of the automatic stay in bankruptcy, the provision of adequate protection payments pursuant to an adequate protection order, and the insufficiency of those payments to compensate Respondent for the actual diminution in value of its collateral during the pendency of the bankruptcy case.

The central holding of the *Vanston* opinion therefore remains applicable:

> In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state where it sits. *Erie Co. v. Tompkins,* 304 U.S. 64, 58 S. Ct. 817, 82 L. Ed. 1188, 114 A.L.R. 1487, has no such implication. That case decided that a federal district court acquiring jurisdiction because of diversity of citizenship should adjudicate controversies as if it were only a state court . . . *But, bankruptcy courts must administer and enforce the Bankruptcy Act as interpreted by this Court in accordance with authority granted by Congress to determine how and what claims shall be allowed under equitable principles.* (Emphasis supplied.)

Vanston, 329 U.S. at 162-163, 67 S.Ct. at 240 (1946).

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[24] *See* Respondent's Brief of Appellee (R-1-2-42), Respondent's Brief in Response to Petitioner's Reply (R-2-7-11), and the District Court's January 31, 1992 Order (R-2-10-7), Appendix B of the Petition, pages 19a through 29a, for detailed interpretation and clarification of this opinion and its progeny.

Accord, In re Blehm Land & Cattle Co., 859 F.2d 137, 142 (10th Cir. 1988), which held that even if a secured creditor failed to seek court approval of its adequate protection agreement with the bankruptcy trustee/debtor, it was not fatal to the creditor's application for a superpriority administrative expense pursuant to 11 U.S.C. § 507(b):

> In drafting this provision (11 U.S.C. § 507(b)), Congress was concerned that the estate would not have sufficient property to pay administrative expenses in full, thus making such adequate protection valueless. *See* S. Rep. No. 989, 95th Cong., 1st Sess. 54, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 5840. *Evidencing the importance with which it viewed the concept of adequate protection, Congress did provide in § 507(b) that, when adequate protection fails, the creditor is entitled to a superpriority administrative claim, above all other regular administrative claims.* (Emphasis supplied.)

The Petitioner simply misreads the *Vanston* case.

CONCLUSION

For the reasons succinctly stated in Respondent's Summary of Argument, *supra*, and based upon the misguided factual and legal assertions made by Petitioner, Respondent respectfully urges that the Petition be denied.

Respectfully submitted,

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